

**Statement by the Gas and Electricity Markets Authority of Yorkshire
Electricity Distribution plc's and Northern Electric Distribution Limited's
non-compliance with Standard Condition 49 of their Electricity
Distribution Licences**

6 June 2007

Summary

1. The Gas and Electricity Markets Authority ("the Authority") grants licences pursuant to the Electricity Act 1989 (the "Act"), inter alia, authorising the distribution of electricity. It has a duty to keep under review activities in the areas to which electricity licences apply. It also has a duty to issue an order to secure compliance where it is satisfied that a statutory or licence obligation is being, or is likely to be, contravened and may impose a financial penalty in respect of a past or continuing contravention.
2. Yorkshire Electricity Distribution plc ("YEDL") and Northern Electric Distribution Limited ("NEDL") are electricity distribution licensees owned by CE Electric UK ("CE"). CE is a wholly-owned subsidiary of MidAmerican Energy Holdings Company.
3. Standard licence condition 49 ("SLC49") of the distribution licence requires the licensee to record and report to the Authority certain information regarding its quality of service performance. The information collected under SLC49 is then used to monitor and determine the licensee's performance in a number of areas, namely customer interruptions (that is, interruptions in the supply of electricity to customers through the licensee's distribution system), customer minutes lost (that is, the duration of loss of supply to customers as a result of those interruptions) and the quality of the licensee's telephone response to calls to its enquiry service. Financial incentives apply to these measures such that distribution companies are exposed to penalties and may gain rewards.
4. CE voluntarily approached Ofgem in August 2006 and disclosed that they had discovered misreporting of interruptions data required under SLC49 paragraph 5(b) for YEDL in the reporting years 2004/05 and 2005/06 and for NEDL in 2005/06.
5. Following their own internal investigation, CE subsequently came forward in October 2006 and disclosed that they had also discovered misreporting of telephony information required under SLC49 paragraph 5(a), for YEDL and NEDL covering the full reporting years 2004/05 and 2005/06 and part of the 2006/07 reporting year.
6. Following the investigation by Ofgem, the Authority found that YEDL and NEDL had breached SLC49 by failing to comply with their reporting obligations in 2004/5 and 2005/6. Misreporting of information is a serious matter especially where it would affect the charges paid by consumers. The Authority may impose a financial penalty where it is satisfied that a relevant licence condition has been breached¹.
7. The specific circumstances of this case are relevant to the consideration of a financial penalty. Having discovered the misreporting CE took

¹ Section 27A of the Electricity Act

independent action to address the problem, bring an end to the breach and to report the matter to Ofgem. Appropriate action was taken with respect to the staff concerned. CE also separated the staff responsible for delivery of network services from those reporting the performance to reduce the incentive for misreporting. New procedures were introduced to provide for greater management oversight of reporting to Ofgem. Furthermore, CE took steps to ensure that customers were not disadvantaged as a result of the misreporting.

8. As a result, in lieu of a financial penalty under section 27A of the Electricity Act, the Authority agreed to introduce modifications to YEDL's and NEDL's licences, which:
 - a. correct the full £5.5 million impact of the misreporting; and
 - b. subject YEDL and NEDL to the reduction of a total sum £2.1 million from the revenues to which they would be entitled if they had correctly reported. This has the effect of a financial sanction².
9. The revenue from a financial penalty imposed under s 27A of the Act goes to the Treasury's consolidated fund. The licence modification has an advantage of reducing CE's revenue, which is beneficial to CE's customers. However, this does not mean that the Authority will not impose financial penalties in any future cases involving misreporting. The Authority's decision in this case reflects its specific circumstances.

Ofgem's investigation

10. As a consequence of the disclosures by CE, Ofgem has conducted an investigation into YEDL's and NEDL's compliance with paragraphs 2 and 5 of SLC49 of their distribution licences. In summary, the investigation has focussed on:
 - discrepancies in the reporting of interruptions data;
 - discrepancies in reporting customer contacts for telephony surveys;
 - the reasons for and consequences of these discrepancies; and
 - the nature and adequacy of the steps taken by CE to prevent recurrence.
11. Statutory requests for information under section 28 of the Act were issued to YEDL and NEDL on 29th November 2006 and 4th January 2007 in respect of interruptions and telephony data respectively. These requests covered a significant range and volume of information relevant to the companies' possible breaches of SLC49.
12. Between August 2006 and April 2007, Ofgem made a number of further enquiries of CE to establish the position with regard to YEDL and NEDL's possible non-compliance with SLC49 of their distribution licences. In January 2007, Ofgem visited CE's offices to audit a sample of the interruptions data that had not been previously disclosed. Ofgem also discussed the steps CE had taken to prevent recurrence and CE demonstrated some of the new processes it had adopted.
13. In May 2007, Ofgem's investigation team presented a statement of case to the Authority which had been seen and commented on by CE on behalf of YEDL and NEDL in accordance with Ofgem's enforcement procedures. The

² Pro-rata on customer numbers, £1.2m to YEDL and £0.9m to NEDL.

statement of case summarised the relevant licence obligations and went on to describe the information provided by CE, Ofgem's analysis of it and conclusion that YEDL and NEDL had breached those obligations but the breaches were not continuing.

14. The investigation report highlighted the following areas of alleged licence breach:

SLC49, paragraph 2 provides: "The licensee shall establish and maintain appropriate systems, processes and procedures to measure and record specified information from the dates specified in paragraph 4 and in accordance with the regulatory instructions and guidance (including any associated information specified therein) for the time being in force pursuant to this condition ("the quality of service rigs")."

Ofgem's statement of case concluded, based on the evidence summarised below, that YEDL and NEDL had breached this aspect of SLC49 due to a failure to maintain appropriate systems, processes and procedures accurately to measure and record specified information during the reporting years 2004/05 and 2005/06. In this regard, the companies:

- re-categorised as "not-reportable" over 4,000 low voltage (LV) faults recorded in their fault reporting system on the basis that there was no outstanding paperwork relating to these records, when this subsequently turned out not to be the case;
- introduced an automated process to suppress uncompleted electronic fault records over one month old;
- did not have in place adequate processes and procedures to record pre-arranged outages;
- did not have in place adequate processes and procedures to check the validity of manual suppressions at high voltage (HV); and
- had operating processes and procedures which meant that not all the relevant telephony data that should have been sent was sent to Ofgem's telephony agent.

SLC49, paragraph 5(a) requires the licensee to provide to the Authority, in respect of each call to its enquiry service, the telephone number of the caller, the time of the call and, if known, the name of the caller and whether s/he is a domestic customer. The licensee is required to do so within four days of the end of the week in which the customer contacted its enquiry service.

Ofgem's statement of case concluded, based on the evidence summarised below, that YEDL and NEDL had breached this aspect of SLC49 due to a failure to provide to Ofgem all the required telephone numbers of such callers within the said timescale.

In this regard, the companies:

- classed "irate" customers as ex-directory so that they would not be sampled as part of the telephony survey undertaken on behalf of Ofgem; and

- filtered out additional categories of customers before sending the customer lists to Ofgem's telephony agent.

SLC49, paragraph 5(b) requires the licensee to report to the Authority by 30th April each year (in respect of the preceding 12 months), inter alia, the number of customers whose supply of electricity was interrupted for three minutes or more and the duration of the interruption.

Ofgem's statement of case concluded, based on the evidence summarised below, that YEDL and NEDL had breached this aspect of SLC49 due to a failure to provide Ofgem with complete data showing the number of customers whose supply of electricity was interrupted for three minutes or more and the duration of the interruption by the 30th April 2005 in relation to YEDL's 2004/05 data and 30th April 2006 in relation to YEDL and NEDL's 2005/06 data.

In this regard:

- CE disclosed to Ofgem on 7th August 2006 that they had discovered a number of incidents which they had failed to include within YEDL's reported figures for 2004/05;
 - CE disclosed to Ofgem on 10th August 2006 that they had also under-reported YEDL and NEDL's interruptions performance data in 2005/06; and
 - Ofgem analysed the information provided by CE, audited the interruptions data originally withheld and concluded that a significant portion of the data should have been provided in accordance with this paragraph.
15. Ofgem operates a financial incentive scheme which rewards companies with a high quality service, which includes fewer customer interruptions and good handling of telephone complaints.
 16. The statement of case set out that Ofgem's assessment of the consequences of these alleged breaches was that, if uncorrected the companies' customers would have paid up to £5.5 million more under the financial incentive scheme than they should have paid had complete and correct information been reported in accordance with SLC49. Ofgem noted that CE had already corrected £4.9 million of this £5.5 million in its revenue returns submitted in August 2006. This adjustment fully reflected the amount by which CE, at that date, thought its prior submissions had been incorrect. A further £0.3 million of the difference would fall to be reported in the revenue returns due in July 2007.
 17. The statement of case also set out Ofgem's assessment that CE had taken appropriate steps to change its processes to achieve compliance with SLC49 and to protect against a recurrence of misreporting.
 18. The statement of case recommended that the Authority find that YEDL and NEDL had breached SLC 49 and that agreed modifications to YEDL's and NEDL's licences should be made in order to:
 - (a) ensure that the companies' customers are no worse off than had the breaches not occurred (by ensuring implementation the full £5.5 million reduction in revenue relative to the original position reported

- by them), thereby correcting the financial consequences of the misreporting; and
- (b) subject YEDL and NEDL to the reduction of a total sum of £2.1 million from the revenues to which they would be entitled if they had correctly reported. This has the effect of a financial sanction³.

CE's response

19. In response to Ofgem's statement of case, CE provided a written submission to the Authority on 3 May 2007. In its written submission, CE confirmed that it:
- did not dispute the facts in the investigation statement of case;
 - did not dispute that breaches of SLC49 occurred;
 - did not dispute Ofgem's assessment of the consequences of the breaches; and
 - would accept licence modifications as outlined in paragraph 13 above.

The Authority's decision

20. On 15 May 2007, the Authority found that YEDL and NEDL had breached SLC49 of their distribution licences by failing to comply with their obligations under paragraphs 2 and 5 of that condition, in 2004/05 and 2005/06.
21. The Authority decided to propose modifications to YEDL's and NEDL's licences, which:
- correct the full £5.5 million that their misreporting would have yielded; and
 - subject YEDL and NEDL to the reduction of a total sum of £2.1 million from the revenues to which they would be entitled if they had correctly reported. This has the effect of a financial sanction⁴.

Further comment

22. The Authority decided not to impose a financial penalty under section 27A of the Act due to the specific circumstances of this case. These include:
- CE took independent action to investigate and address the misreporting, including taking appropriate action with respect to the staff concerned;
 - CE ended the breach by introducing new procedures, which provide greater management oversight and by separating the service delivery from performance reporting; and
 - CE came forward to report the breach to Ofgem; and
 - CE fully co-operated, took steps to ensure that customers were not disadvantaged as a result of the misreporting and accepted the recommendations of the investigation.
23. Unlike a financial penalty imposed under section 27A of the Act, the licence modifications reduce CE's revenue and benefit CE's customers. This does not mean that the Authority will not impose financial penalties in respect of any other cases of misreporting. The Authority's decision in this case reflects its specific circumstances.

³ Pro-rata on customer numbers, £1.2m to YEDL and £0.9m to NEDL.

⁴ Pro-rata on customer numbers, £1.2m to YEDL and £0.9m to NEDL.