

**Financial penalty decision by the Gas and Electricity Markets Authority,  
following a finding of breach by Northern Gas Networks Limited with its  
obligations under Standard Special Licence Condition D10 of the Gas  
Transporters Licence**

**4 February 2008**

**1. Summary**

1.1 On 19 December 2007, the Authority published its decision that Northern Gas Networks (NGN) had contravened its obligations in SSLC D10 (2) (b), (c) and (e) and, in accordance with section 30 A(3) of the Act, gave notice of its intention to impose a financial penalty of £25,000 on NGN, for the reasons set out in section 6 below. The Authority has received no representations or objections in response.

1.2 The Authority now therefore gives notice of confirmation of that penalty, in accordance with section 30A(5) of the Act.

1.3 NGN is a licensed gas transporter company which serves the north of England. It is owned by a consortium of six partners, including United Utilities plc. As a licensee, NGN is obliged to comply with the conditions of the Gas Transporters Licence. Licence condition SSLC D10 imposes obligations on NGN regarding certain connections activities (including the provision of quotations for connections work within particular timescales and the provision of dates for the commencement and substantial completion of the work).

1.4 In the autumn of 2006, NGN informed Ofgem that it was experiencing difficulty in meeting certain of its obligations under SSLC D10, in particular the obligations at SSLC D10 (2)(b), (c) and (e).

1.5 NGN explained that these difficulties had arisen following its having given notice to its service provider in order to bring its connection business in-house to be managed by an operating company, United Utilities Operations Limited ("UUOL"), from 31 July 2006. UUOL is a subsidiary of United Utilities plc, one member of the consortium which owns NGN. On 31 March 2007, NGN submitted statistical reports to the Authority which confirmed that it had failed to meet its obligations under SSLC D10 (2) (b), (c) and (e).

**2. Background**

2.1 SSLC D10 places obligations on licensees to meet certain standards relating to connections to the gas pipeline network.

2.2 The relevant parts of SSLC D10 are as follows:

"(2) The licensee shall procure that:...

(b) 90% of non-standard quotations for:

(i) obtaining a new connection or altering an existing connection up to and including rates of flow of 275kWh per hour are issued within eleven working days of receipt of the request unless the customer requests a deferral; and

(ii) obtaining a new connection or altering an existing connection where rates of flow exceed 275kWh per hour are issued within twenty one working days of receipt of the request unless the customer requests a deferral;

(c) 90% of new or altered connections are substantially completed within the timescales agreed with the customer;...

(e) in 90% of cases, provide within twenty working days dates for commencement and substantial completion of works from the receipt of acceptance of a quotation provided under paragraph 2 (a) or (b) unless the customer requests a deferral."

2.3 In addition to having to meet these requirements under the Gas Transporters Licence, the Gas (Standards of Performance) Regulations 2005<sup>1</sup> ("the Regulations") require gas transporters to meet the same obligations in respect of each individual customer. The Regulations also require the gas transporters to pay the relevant customer for any failure to do so.

2.4 In June 2005, ownership of NGN passed from National Grid Transco to a consortium. There was a pre-existing contract in place with another provider for the provision of connections services, which terminated on 30 July 2006.

2.5 At a meeting with Ofgem on 10 October 2006, prompted by NGN, the company explained difficulties which it was experiencing in meeting the obligations at SSLC D10 (2) (b), (c) and (e).

2.6 On 31 March 2007, NGN submitted statistical reports to the Authority which confirmed that it had failed to meet its obligations under SSLC D10 (2) (b), (c) and (e). NGN has subsequently submitted statistics for the quarter ending 30 June 2007, which show that it was meeting or exceeding the standards set in SSLC D10. Therefore, the contravention is no longer ongoing. All relevant statistics are set out in Table 1.

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<sup>1</sup> Regulation 10 and Pt I of Schedule I of the Gas (Standards of Performance) Regulations 2005, SI 2005/1135, pursuant to section 33AA of the Gas Act 1986

**Table 1 Compliance with SSLC D10**

<b>Provision</b>	<b>Relevant Conditions</b>	<b>Target</b>	<b>Annual performance achieved 2006-07</b>	<b>Annual performance achieved Q1 2007-08</b>
Provision of non-standard quotations for obtaining a new connection or altering an existing connection < 275 kWh within 11 working days	SSLC D10(b)(i) Gas Regulation 10(3)(b)(i) (Standard 5)	90%	<b>76.1%</b>	<b>95.9%</b>
Provision of non-standard quotations for obtaining a new connection or altering an existing connection > 275 kWh within 21 working days	SSLC D10(b)(ii) Gas Regulation 10(3)(b)(ii) (Standard 6)	90%	<b>84.4%</b>	<b>97.5%</b>
Provision of a date for commencement and substantial completion of relevant works within 20 working days	SSLC D10(c) Gas Regulation 10 (3)(e) (Standards 9 & 10)	90%	<b>69.0%</b>	<b>90.1%</b>
To substantially complete connection works within timescales agreed with customer	SSLC D10(e) Gas Regulation 10(3)(f) (Standard 11)	90%	<b>86.9%</b>	<b>93.1%</b>

### **3. Ofgem's investigation**

3.1 Following NGN's admission that it was experiencing difficulties in late 2006 Ofgem met with NGN on four occasions between October 2006 and April 2007 to discuss the problems with its performance following the transfer of its connections services.

3.2 In July 2007, Ofgem wrote to NGN confirming that it had commenced a formal investigation into the company's compliance with SSLC D10, enclosing a formal information request pursuant to section 38 of the Act.

3.3 NGN responded in August 2007, acknowledging that NGN had contravened licence requirements in relation to connections activities. A Statement of Case was issued to NGN in October 2007, setting out the Ofgem case team's view that NGN had breached its obligations under SSLC D10 of its licence and indicating that, in its view, a low level penalty would be appropriate if the Authority found that a breach had occurred.

#### **4. Summary of Ofgem's statement of case**

4.1 Ofgem's Statement of Case set out the key points cited by NGN as underlying its breach of the obligations.

4.2 The problems experienced by NGN arose as a result of unexpected problems with the transfer of its connections business in-house. NGN had taken a number of steps to ensure an orderly transition. It forecast that a workload of around 1,000 planned and accepted jobs (approximately 3 weeks work) and around 270 calls per day would be transferred.

4.3 NGN built in a contingency of 20 per cent extra resources over the first two years of the changed arrangements. However, it transpired that the volume of work had been underestimated and that the contingency planning undertaken by NGN was inadequate to address the resulting difficulties.

4.4 NGN undertook a number of actions to overcome the problems before contacting Ofgem to inform it of the situation, including meeting with key customers when it became clear that problems were being experienced and recruiting extra staff. NGN ensured that Ofgem was made aware of its problems promptly and the actions being taken to resolve them.

#### **5. NGN's comments in mitigation**

5.1 On 30 October 2007, NGN responded to Ofgem's Statement of Case. It acknowledged that it had contravened SSLC D10 and stated that Ofgem's Statement of Case was "a reasonable representation of the facts".

5.2 NGN also set out, in its response, a number of factors in mitigation. It argued that it had built reasonable foreseeable contingencies into its plans for the cutover, including the recruitment of significant additional resources, but these were overwhelmed by the scale of the problems experienced. NGN took active steps to remedy the problems with the deployment of further resources. By March 2007, the business was meeting the standards but there was insufficient time to recover the annual performance position.

5.3 NGN also highlighted that it had paid guaranteed standards of performance payments of £711,067 under Regulation 10 and Pt I of Schedule I to the Regulations, as well as ex-gratia payments of £185,000. In addition, it made payments under the voluntary standards of service scheme for shippers, suppliers, independent gas transporters and utility infrastructure providers, which are covered by the performance standards in SSLC D10. The value of payments made under the voluntary scheme for 2006/07 in relation to the standards in SSLC D10 (2) (b), (c) and (e) was £171,511. NGN submitted that the level of compensation paid to customers exceeded £1m, of which in excess of £350,000 of that amount was paid on a voluntary or ex-gratia basis.

5.4 It submitted that it had suffered a loss of business as a number of major commercial customers withdrew connections work from NGN and placed this with alternative providers.

5.5 NGN stated that it had admitted its problems to Ofgem in an open and transparent manner and kept Ofgem informed of developments. It has also cooperated fully with the investigation and provided all relevant information to the case team.

5.6 Finally, NGN stated that the level of compensation payments which it had made and the damage it had suffered to its reputation were themselves deterrents to other licensees.

## 6. The Authority's Decision

### *Contravention*

6.1 The Authority's decision, published on 19 December 2007, was that a contravention of SSLC D10 had occurred, in that in reporting year 2006/07 NGN failed to comply with the obligations imposed by SSLC D10 (2)(b), (c) and (e). The precise extent of the breach is set out at Table 1 above.

6.2 That contravention was admitted by NGN in its response to Ofgem's Statement of Case<sup>2</sup>.

6.3 The Authority found, further, that the contravention was no longer ongoing, having regard to the statistics provided by NGN for Quarter 1 of the reporting year 2007/08.

6.4 Having made these findings the Authority considered whether it was appropriate to issue a financial penalty and if so, what the amount of that financial penalty should be. For the reasons set out below (paragraphs 6.5 to 6.14 below) the Authority concluded that it would in this case be appropriate to impose a financial penalty of £25,000.

### *Should a penalty be imposed?*

6.5 In its published guidance, the Authority has stated that in deciding whether to impose a penalty, it will have regard to the particular facts and circumstances of the contravention under consideration, including the extent to which the circumstances from which the contravention or failure arose were outside the control of the licensee.

6.6 Having had regard to the Statement of Case, the most relevant factors referred to in the guidance appear in the instant case to be:

- whether the principal objective and duties of the Authority preclude the imposition of a penalty;
- whether the contravention or the failure has damaged the interests of consumers or other market participants; and
- whether or not the contraventions were of a trivial nature.

6.7 There is nothing in the Authority's principal objective and duties to prevent the imposition of penalty in this case. It considers, further, that the contraventions have damaged the interests of consumers because access to gas

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<sup>2</sup> See NGN's response dated 30 October 2007

<sup>2</sup> "Utilities Act: Statement of policy with respect to financial penalties", published by Ofgem in October 2003:

<http://www.ofgem.gov.uk/About%20us/Documents1/Utilities%20Act%20-%20Statement%20of%20policy%20with%20respect%20to%20financial%20penalties.pdf>

supplies was delayed. They cannot be described as “trivial”, since they affected some 36,500 customers.

6.8 Accordingly, the Authority concluded that it was appropriate to impose a financial penalty in this case.

#### *Amount of penalty*

6.9 According to its published guidance, the Authority is required to have regard to various factors in determining the amount of any penalty, including:

- the seriousness of any contravention or failure;
- the degree of harm or increased cost incurred by consumers or other market participants after taking account of any compensation paid;
- the duration of the contravention or failure;
- the extent of any attempt to conceal the contravention or failure from Ofgem;
- the extent to which the licensee has been taking steps to secure compliance, either specifically or by maintaining an appropriate compliance policy, with suitable management supervision;
- reporting the failure to Ofgem; and
- co-operation with Ofgem’s investigation.

6.10 The extent of any financial detriment to customers is unclear. However, other forms of detriment are likely to have occurred (e.g. inability to occupy property or operate businesses). This detriment will have been to some extent offset by statutory or ex-gratia payments which NGN state exceeded £1m. There is no evidence to suggest that NGN profited from the contraventions, and indeed it has asserted that it has lost business as a result.

6.11 NGN had taken reasonable steps to secure compliance, including the development of contingency plans relating to the transfer of its connections business in-house. It also took prompt additional steps to deal with the problems which it experienced.

6.12 The service failures related to the period of 9 months from June 2006 to March 2007. NGN now appears to be meeting the standards.

6.13 There was no attempt to conceal the contravention; NGN reported and discussed its failures promptly and co-operated fully with Ofgem’s investigation.

6.14 In all the circumstances of the case and having regard to the mitigating factors identified by NGN, the Authority’s reached the view that a penalty of £25,000 was appropriate.

#### *Notice of financial penalty*

6.15 As required by section 30A(3) of the Act, the Authority on 19 December 2007 gave notice of its intention to impose a financial penalty of £25,000 on NGN in respect of the contravention. It set out the reasons (listed above) for reaching that decision. The notice indicated that any representations

or objections should be sent to the Authority by 18 January 2008, which was 30 from the date of the notice.

6.16 The Authority has received no representations or objections in response.

*Conclusions*

6.17 The Authority has, for the reasons stated above, decided to impose a financial penalty, of £25,000 on NGN under section 30A (1) of the Act, in respect of the contravention of its obligations in SSLC D10(2)(b),(c) and (e).

6.18 The penalty must be paid to the Authority no later than 17 March 2008, which is 42 days from the date of this notice.

A handwritten signature in black ink, appearing to read 'S Smith', written in a cursive style.

**Steve Smith**  
**Managing Director Networks**  
**Ofgem**

This decision, and the associated recommendations, were made by Steve Smith, the Managing Director of Ofgem Networks, under powers formally delegated to him for this purpose by the Authority.