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Dear Anna,

**Draft Enforcement Guidelines for Complaints and Investigations ("the Draft Guidelines")**

Thank you for the opportunity to provide comments on the above document, which Ofgem published for consultation on 16 December.

Our comments are as follows:

Enforcement Strategy

Ofgem's enforcement approach should be informed by other work being carried out on regulatory enforcement. For example, the recent discussion document by BIS entitled "Transforming Regulatory Enforcement"[1], which encourages a "new relationship between regulators and businesses where the default setting is trust rather than distrust". We think that this objective seeks to promote a positive relationship between the regulator and the companies it regulates. As such, we would expect increased dialogue and co-operation between Ofgem and regulated companies rather than a prescriptive approach, which encourages an adversarial relationship between the parties.

With this in mind, in our review of the draft guidance we note that the process (as set out on page 25) does not build in any opportunity for engagement between the investigative team and the company prior to the issuing of the Statement of Case. We consider that, during the

[1] Transforming Regulatory Enforcement: Freeing up Business Growth – June 2011. In this document, BIS sets out three key principles for enforcement, as follows:

- Greater accountability (i.e. accountability of the regulator to the regulated companies)
- Recognising and promoting good practice (i.e. requiring regulators to take account of companies efforts to comply)
- Greater transparency

investigation and before the issuing of a Statement of Case, Ofgem should set out its initial findings and provide the parties with an opportunity to proactively address the key issues identified. This could be achieved through a meeting prior to the issue of the Statement of Case. We think that including such a process will allow Ofgem to better refine its case, as well as helping to inform the regulated party regarding what the perceived areas of weakness are and how these could be addressed in practice.

This point is particularly relevant to the Information Request process (discussed more particularly below). There may be a substantial delay between the licensee responding to the Information Request and Ofgem producing the Statement of Case. During this delay, the licensee may well have made improvements to their processes. Better communication between Ofgem and the licensee during this period would ensure that any such improvements are informed by Ofgem's ongoing investigation. Equally, this will allow Ofgem to ensure that the Statement of Case is informed by the licensee's current processes, as well as the historical position covered by the Information Request.

Information Requests

As set out in section 4.6 of the draft guidance, the initial stage of an investigation will involve formal Information Requests (IR). Ofgem needs to recognise that the time and resource required in order to prepare a response to an IR can be an onerous regulatory burden, particularly where the scope of the IR is wide. In some cases, an IR may involve compiling hundreds of documents for submission to Ofgem or will necessitate an internal investigation. Currently, there is little guidance regarding how Ofgem will use its IR powers in practice. In particular, it would be useful if a minimum period of time was agreed in the guidance for the submission of a response, as well as a recognition that complex/widely framed IRs will require more time than simple/focused IRs.

Enforcement and Industry Code Compliance

We do not consider that the Draft Guidelines provide enough clarity as to how Ofgem will approach the concurrent powers of the Authority and the various Code bodies in relation to enforcement. The fact that market participants may face enforcement action from two separate parties creates uncertainty for market participants. There is currently a lack of clear concurrency rules. While this dual enforcement role continues without proper concurrency procedures in place, there is a potential for "double jeopardy", which may threaten procedural fairness.

In our response to the consultation on the previous enforcement guidelines, we took the view that Ofgem should review its role in overseeing the industry codes. We continue to believe that such a review would be appropriate.

Financial Penalties Guidance

There are several references to penalties in the Draft Guidelines, an issue which is covered in a statutory Statement of Policy drafted by Ofgem under section 27B of the Electricity Act (section 30B of the Gas Act). This guidance is dated 2003 and has not been updated since it was first issued. We assume that the current Draft Guidelines have been drafted in a way that

is consistent with the Statement of Policy, however we would query why this has not been reviewed by Ofgem as part of the current workstream in order to ensure that it is fully up-to-date with modern regulatory enforcement policies and best practice/Better Regulation.

Competition Enforcement: Other Guidelines

The Draft Guidelines cover Ofgem's full range of investigatory powers, covering off regulatory, Competition Act and Enterprise Act powers. Whilst we appreciate the current guidance also covers this same wide range, we would suggest, given the complexity of Ofgem's competition law powers and, in particular, the concurrency arrangements with the OFT, that separate guidance is produced dealing with Ofgem's Competition law and Enterprise Act powers.

We note that there is pre-existing guidance on the enforcement of competition law in the energy sector, which was co-written between Ofgem and the OFT (Ref: OFT428). These are referenced in the Draft Guidelines (para. 1.13). Rather than having 2 or more sets of guidance on the same topic, we consider that it would be in the interests of Better Regulation to consolidate the competition law guidance into one stand-alone document co-published by OFT and Ofgem. This will avoid the potential for overlapping and potentially contradictory guidance on this complex topic, as well as removing the need for market participants to cross-refer between documents. As OFT428 is now several years old (it is dated 2005), we consider that it is appropriate that these guidelines are now updated.

The Settlement Procedure

It appears that Ofgem is seeking to formalise settlement negotiations as a stage in its enforcement procedure. Whilst we recognise that settlement negotiations will inevitably play a part in some investigations (e.g. in cases where both parties are in agreement as to liability and that the proposed penalty is reasonable in all the circumstances of the case), we are not convinced that this should be a formal stage in Ofgem enforcement actions.

Ofgem explains that the purpose, or the attraction, of the settlement procedure is a means for the licensee participating in the settlement negotiation to achieve a lower penalty than that which would be imposed by an Enforcement Committee and that "the sooner settlement is reached the more significant any reduction in penalty is likely to be". We have two observations to make on this: (i) by introducing a type of "early bird discount" on penalties, this intended approach may place unreasonable pressure on companies to settle early in the process and may result in the acceptance by companies of an inappropriate outcome rather than risk the relative uncertainty of the Enforcement Committee; and (ii) there is a clear statutory framework for the imposition of penalties and we do not think that there is any legal basis for the introduction of a formalised settlement procedure.

Furthermore, the proposed settlement procedure is heavily weighted in favour of Ofgem. The proposed settlement procedure places pressure on the licensee to enter settlement negotiations, while allowing Ofgem the freedom to decide whether the case is suitable for the settlement procedure or not. Ofgem can consider "a range of factors" when deciding whether the case is suitable, however no indication is provided regarding what these factors might be. We would also note that proceeding by negotiated settlement effectively cuts off, or

significantly reduces, a licensee's opportunity to appeal a penalty decision or raise judicial review. We are concerned that formalising the settlement procedure places an unreasonable pressure on companies to proceed down a route which will adversely affect their legal rights to challenge Ofgem.

The introduction of the settlement procedure threatens to add an opaque layer to the enforcement procedure, which we think will create uncertainty for licensees. Without clear visibility regarding how Ofgem will conduct itself during the settlement procedure, licensees will have no comfort that Ofgem is taking a proportionate approach or acting consistently when undertaking action against several licensees. In short, we consider that this proposed aspect reduces transparency and is therefore in conflict with one of the key regulatory enforcement principles set out by BIS in its recent paper on regulatory enforcement (referred to above).

Provisional Orders

Provisional Orders may be imposed with the minimal process requirements (for example, there is no statutory appeal route). For this reason, we consider that Provisional Orders are a draconian measure and should be reserved for situations where other avenues of redress have been exhausted. Before issuing a provisional order, Ofgem should first provide the licensee with an opportunity to take steps to voluntarily address the alleged detriment. Engaging with the party concerned will enable less onerous options to be explored. If the circumstances do not allow time for formal engagement with the party concerned, then this should be done informally prior to the imposition of the Order.

Furthermore, Ofgem should ensure that the decision to impose a Provisional Order should be taken, at the very least, by someone at Senior Partner level who is not directly involved with the investigation. This will help ensure that the decision has been taken impartially, which best promotes procedural fairness. As Ofgem is undertaking a quasi-judicial function, it should be seeking to replicate similar safeguards as would be expected by a party facing an injunction in Court.

Response to Statement of Case

Under the current process, Ofgem is given 9 months (or more) to investigate and prepare a statement of case, whereas the party concerned is generally allowed 21 days. In this time, a party will review the statement of case; consider the evidence produced by Ofgem; undertake internal investigations; and draft a formal response. In some cases, a party may also wish to obtain legal advice regarding the statement of case. 21 days is not enough time particularly when considering that during the oral Enforcement Hearing, a party is not entitled to introduce any further material (see para. 4.38) and there is no formal process for adjustment of the written case. A party must be given a fair opportunity to prepare a defence. We would suggest that 6 weeks (42 days) is a more appropriate standard period of time, with more complex cases being granted at least 8 weeks (56 days).

Supplementary Statement of Case

The procedure allows Ofgem to issue a supplementary Statement of Case, with the opportunity for response from the licensee also built into this process. We consider that there should be an equal opportunity for the licensee to issue a supplementary Response, regardless of whether a supplementary Statement of Case has preceded it. This is especially important given the short period of time allowed under the current drafting of the procedure for a Response (discussed above). This will help address the imbalance that exists between Ofgem and the licensee in relation to case preparation time.

Communication during the Enforcement Process

There is no limit to the length of time that Ofgem may take to complete its investigation. Though Ofgem aims to either progress to a statement of case, or close the investigation within 9 months, the guidance leaves open the possibility that the timescales may be longer. We consider that communication throughout the enforcement process is important to achieve transparency. Rather than one update in 9 months (as currently set out in the draft guidelines), we think that the process should include the requirement to provide regular updates. This is related to our point regarding the need for greater engagement, mentioned above.

Oral Representations

We note that paragraph 4.38 provides that "the company should not introduce any new material". This should read "neither the company nor Ofgem should introduce any new material".

I hope the foregoing is helpful. If you would like to discuss any of the above comments in more detail then please contact me.

Yours sincerely,

Lesley Gray
**Regulation**