

29 May 2013

Megan Forbes
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Dear Megan,

Review of Ofgem's enforcement activities – consultation on strategic vision, objectives and decision makers

We welcome the publication of Ofgem's consultation on its strategic enforcement vision, objectives and decision making and support most of the proposals within the document. A transparent and well understood enforcement regime is a prerequisite for a stable and properly functioning retail market.

The introduction of Ofgem's new Standards of Conduct ('SOC') means that this review is particularly timely. We broadly welcome Ofgem's proposed structural changes, but, as already discussed with you, we believe the most important changes are those that support the advent of the Standards of Conduct; particularly, those underpinning the evolutionary implementation of the SOC. Embedding the SOC into working practices and culture will be a major undertaking. Clarity from Ofgem on how the SOC will be enforced and ongoing dialogue on how suppliers can comply with the SOC is essential.

Our detailed responses to Ofgem's specific questions are set out in the annex to this letter. We have also highlighted below a number of key points that we urge Ofgem to consider when implementing the changes from this review. Specifically, we hope the review will deliver / enable:

- a consistently applied approach across all licensees and areas of Ofgem's enforcement work under different powers which reinforces the Better Regulation Principles¹, including a mechanism to discuss and compare enforcement decisions in line with Ofgem's new Vision, Objectives and Strategic Priorities;
- a clearer and more accurate understanding of consumer behaviours and issues by more closely aligning enforcement and policy teams;
- a culture change – in both Ofgem and licensees – where open dialogue on compliance complements proportionate and timely enforcement action that is well communicated, understood and predictable, particularly whilst the SOC are being implemented;
- clearly documented guidance and procedures outlining the steps, outcomes, timescales and responsibilities at each stage of the enforcement process;
- a fair, independent and objective process to clearly demonstrate the steps taken in arriving at a decision;
- a level playing field for all licensees – irrespective of size – that is proportionate and reflects the seriousness of the breach;
- a forward-looking approach leading to better judgements about the problems that drive poor consumer outcomes and identify future risks before they occur;

¹ <http://www.bis.gov.uk/brdo/resources/knowledge/better-regulation-principles>

- a culture and framework where lessons are more easily learned from enforcement action, helping licensees to comply with relevant regulations more effectively and efficiently; and
- a clearer framework and process for settlement discussions, which are documented and well understood from the outset by all parties.

As part of this review, we hope that Ofgem makes the changes necessary to afford licensees and consumers with greater clarity and transparency about the purpose of Ofgem's enforcement actions and choices. An important part of this will be making a clearer distinction between compliance and enforcement; increased compliance dialogue in particular will, over time, lead to a far more transparent, effective and efficient enforcement framework.

I hope that you find these comments helpful and I look forward to discussing the findings of the second stage of Ofgem's Enforcement Review later in the summer. In the meantime, please do not hesitate to contact me if you would like to discuss any aspect of this response.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Tim Dewhurst', with a stylized, cursive script.

Tim Dewhurst
Director, Regulatory Affairs
British Gas

Annex – detailed responses to Ofgem’s questions

Q1. Do you agree that this is the right Vision for Ofgem’s enforcement work? Please provide us with any comments you have on the Vision; and

Q2. Do you agree with Ofgem’s proposed Strategic Objectives, and principles for achieving them, and do you think it would be helpful to adopt annual strategic priorities? Please explain the reasons for your answer and any aspects which you think we should consider.

1. Ofgem’s new Vision alongside the revised Objectives and Strategic Priorities are appropriate, and should provide an appropriate focus on delivering outcomes that are in the interests of consumers. We also agree that, in the current climate of unprecedented levels of uncertainty and change, annual strategic priorities would be helpful in increasing the stability and predictability of the enforcement framework.
2. On an ongoing basis, we would ask that Ofgem regularly reviews its goals and strategic priorities to ensure that they meet the constantly evolving needs of customers. This review represents an opportunity to do this afresh with licensees. Ofgem’s strategic priorities are an important influence on the way in which compliance resource is allocated by licensees, particularly with the implementation of SOC. These should therefore be determined in a thoughtful and considered way, and where appropriate, reflect feedback from engagement with key stakeholders including licensees and consumer organisations.
3. Mechanisms for effective stakeholder engagement (including direct engagement with consumers where appropriate) are already practiced by other regulatory bodies. The FCA, for example, has a separate department devoted to understanding the issues which are facing customers and the relevance of this to the actions of licensees, enabling it to:
 - shape and deliver its strategic priorities through its policymaking, supervision approach and enforcement activities more effectively;
 - develop a measured enforcement approach based on a proper understanding of the issues and a full consideration of the potential solutions;
 - shift resources to allow it to deal more quickly and effectively with emerging issues;
 - run more cross-industry projects to get to the root cause of problems; and
 - work with licensees to make regulation work better and give room to try new ideas and commercial propositions when it is in customers’ interests to do so
4. It is important that Ofgem’s proposed Strategic Objectives (and its enforcement approach more generally) should be applied on a consistent basis when Ofgem is considering using any of its powers. This includes licence breaches, new powers such as REMIT, proposed powers to award consumer redress under both the Energy Bill and the Consumer Bill of Rights and, as far as possible, the way in which Competition Act cases will be decided in the future and any changes following reform to the competition regime arising from the Enterprise and Regulatory Reform Bill.
5. It would be useful if Ofgem had arrangements in place to discuss and compare enforcement decisions in line with Ofgem’s new Vision, Objectives and Strategic Priorities. This will help Ofgem to set its strategic enforcement priorities, which we believe should be reviewed annually, consulted on and published, and identify areas of particular concern. It will also help Ofgem in dealing with contested and settled cases.
6. Consistency and benchmarking should be important aspects of the enforcement process to ensure that there is a level playing field for all licensees – irrespective of size. Action should be taken where a material breach has occurred, but it should be proportionate and reflective of the seriousness of the breach (rather than primarily being driven by other considerations, such as the desire to deter other offenders). Deterrence can be promoted through richer engagement with licensees on lessons learned, and ongoing compliance dialogue. Regular working groups with suppliers would also be helpful in encouraging a better understanding of what constitutes good practice.

Q3. What obstacles do you consider that Ofgem may encounter in achieving its Vision and Strategic Objectives?

7. The most significant obstacle Ofgem may encounter in achieving its new Vision and Strategic Objectives will be facilitating the necessary change in culture needed for a principles based regulatory regime. This will require a shift away from a current tendency to focus on ensuring technical compliance with a set of prescriptive rules, to one more appropriate to a regime focused on standards of conduct. Conversely, licensees should also expect to see a step change in the behaviour of the Ofgem Enforcement Team, i.e. to deliver against Ofgem's Vision and Strategic Objectives as set out in the consultation paper.
8. Changes in culture take time to fully embed in behaviours, requiring dedicated and persistent focus over a number of years. To achieve its favoured Vision and Strategic Objectives, Ofgem needs to reflect (and support licensees with) these challenges in its enforcement approach. As set out above, ongoing dialogue on compliance (particularly focused on helping licensees to introduce the new Standards of Conduct as efficiently as possible), will help encourage a positive culture change in licensees. Such an approach would not only be mutually beneficial to both Ofgem and licensees, but also, critically, for consumers.
9. As with the FCA model, Ofgem needs to drive forward-looking, mature and open dialogue with licensees in order to make proportionate and considered decisions. This needs to be embedded into the process, again particularly as the Standards of Conduct get implemented, to ensure that Ofgem is able to learn more about suppliers' specific challenges, understand any specific remedial action required, and provide comments and feedback. When enforcement action is being considered, Ofgem should, where appropriate, proactively open discussions, preferably face-to-face, with the affected licensees to openly talk about the nature and scale of the issue, as well as options, next steps and timescales.

Q4. Do you agree with the proposals for an Enforcement Decision Panel and Secretariat to take decisions in contested enforcement cases? Please explain the reasons for your answer.

10. At present, we understand that there is a requirement to separate the activities of the enforcement and policy teams – particularly at a management level – to ensure that any subsequent enforcement activity is not compromised by previous discussions. Whilst this is understandable, it risks a dislocation between the enforcement and policy teams, which is particularly unhelpful at times of important policy change (such as the development and implementation of standards of conduct).
11. To the extent that the development of an Enforcement Decision Panel and Secretariat will introduce safeguards to more tightly “ringfence” enforcement action, enabling closer working between the policy and enforcement teams on a day to day basis, this development is to be welcomed. However, whilst the proposals for an Enforcement Decision Panel and Secretariat to take decisions in contested enforcement cases would appear to enhance the visible separation between the investigation and decision-making functions, we would need more information before we can assess these proposals further.
12. Specifically, there is currently insufficient information for us to understand exactly how and when the process will be used, for example how members will:
 - be recruited to ensure that suppliers have confidence that the work undertaken by these new bodies is robust, and not subjective, inconsistent or formed on conflicting priorities;

- possess the relevant skills and experience to make consistent “customer outcome based” assessments in line with Ofgem’s new Vision, Objectives and Strategic Priorities; and
- apply Ofgem’s new credible deterrence principle when making enforcement decisions.

13. It would also be very helpful if Ofgem could spell out more clearly its thoughts on how this new structure would enable Ofgem to provide more compliance dialogue with both internal policy teams, and external stakeholders (inc. licensees).

Q5. Do you agree with the proposals for settlement decisions? Please explain the reasons for your answer.

14. Yes, we fully support Ofgem’s settlement procedure whereby it should be possible to bring cases to an early resolution by agreement. There are benefits to all parties, with consumers likely to obtain compensation earlier than would otherwise be the case and which saves resources for both the Ofgem and the licensee.

15. We ask Ofgem to seek to use this review to ensure that the benefits of using the settlement process are always clear from the outset, e.g. a reduction in timescales and any penalty imposed. An example of this is the FCA model which operates a discount scheme for early settlement, whereby proactive co-operation is likely to result in reduced financial penalties in the majority of cases. It is applied on a sliding scale, depending on the timing of the settlement, as follows:

- Stage 1 (early settlement stage): 30%
- Stage 2 (up to the expiry of the period for making written representations to the RDC): 20%
- Stage 3 (up to the issue of the Decision Notice): 10%

16. We also agree that:

- decisions on cases which are below the penalty threshold of £100k should be taken by the Senior Partner in charge of enforcement, with advice from an Enforcement Oversight Board made up of Partners from across Ofgem;
- the Board should be a permanent body, which would take strategic decisions on enforcement cases throughout their duration; and
- the same decision-making guidance should be used irrespective of how the decision is made

17. In addition, all settlement communications should be made on a without prejudice basis and if the settlement negotiations break down and the case proceeds through a contested administrative process, any admissions or concessions made during settlement talks should be discounted.

18. It is important that the review delivers a fair, independent and objective process that clearly demonstrates the steps taken in arriving at a decision and avoiding the influence of personal views. There should be clearly documented procedures, preferably in the Enforcement Guidelines, which outline the steps, outcomes, timescales and responsibilities at each stage of the enforcement process, including the roles of Authority, Enforcement Decision Panel and Settlement Committee.

19. There should also be clear guidance on the Authority’s policies on issues such as expected compliance standards, settlement, deterrence and any other relevant matters – including providing guidance when new situations arise or where there is a lack clarity or certainty.

Q6. Do you agree with the proposed arrangements for the Authority’s oversight of the Panel’s work? Please explain the reasons for your answer.

20. Yes, we do agree that the Authority should have strategic oversight of decision-making for both contested and settled cases. Providing guidance to those making decisions in all cases will help to ensure that there is a consistent approach in terms of both direction and decision-making. It will also help to give licensees confidence in the system and, therefore, set the right tone for constructive relationships with licensees.
21. This new guidance is critical in providing a clear framework and embracing Ofgem's Vision by setting the Authority's policies on issues such as standards of compliance expected, settlement, deterrence and any other relevant matters. It should be published and, in our opinion, form part of the Enforcement Guidelines. Licensees require clear, targeted and timely information and guidance.
22. With the introduction of SOC, there is a risk that enforcement decisions could be subjective. To protect against this we believe there needs to be a range of measures to raise merit-based appeals, perhaps similar to those in the financial services sector, including:
- an independent and impartial legal review undertaken in every case;
 - the ability for have an independent review by skilled persons e.g. a big four consultancy;
 - evidence to be considered by a separate "Regulatory Decisions Committee" before a decision is made;
 - access to an appeals tribunal which involves non-Authority representatives;
 - mediation of settlement discussions through a neutral agency;
 - rights of appeal to the High Court; and
 - all mechanisms being underpinned with constant dialogue.

Q7. Do you have any additional comments on the matters covered in this Letter?

23. The points made in this letter compliments and builds on the principles set out in our response to Ofgem's Draft Enforcement Guidelines on Complaints and Investigations, dated 28 February 2012, which outlined our views that Ofgem's approach to enforcement should:
- be clear, fair and proportionate;
 - follow a clearly structured procedure;
 - be applied consistently to all licensees;
 - be consistent with the regulatory approach adopted by other parts of Ofgem;
 - include more constructive engagement prior to enforcement action being taken; and
 - reward proactive engagement through clearly defined procedures