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29 May 2013

Dear Megan,

**REVIEW OF OFGEM'S ENFORCEMENT ACTIVITIES – CONSULTATION ON  
STRATEGIC VISION, OBJECTIVES AND DECISION MAKERS**

Thank you for the opportunity to respond to the above consultation.

We welcome Ofgem's broad intent to review the efficiency of its enforcement policies and procedures and to incorporate them within a transparent strategic framework.

Our responses to the specific questions raised in the consultation are in Annex 1 to this letter. Our key points are as follows:

- We think that the proposed vision for enforcement is broadly appropriate but we think it should be altered to read "to achieve a culture where businesses put *their duties* to energy consumers first and act in line with their obligations". Some aspects of putting consumers first (such as charging low prices or giving excellent customer service) are matters for competition, not enforcement;
- While the strategic objectives and principles for achieving them are all appropriate, we think they are too narrowly focused on deterrence, to the exclusion of constructive engagement. While high profile deterrence may be necessary on occasion, it can also act as a barrier to entry (especially for existing customer-facing brands). Other regulators have recognised the importance of constructive engagement alongside deterrence, and we think the objectives as currently proposed could make it harder to achieve the correct balance. The objectives should make reference to the need to operate a visibly fair and efficient enforcement process to reassure prospective market entrants.
- We can see merits with the proposal to recruit a pool of professional decision makers to deal with contested decisions, particularly if they have some judicial expertise. However, it is not clear to us whether Ofgem's current proposals for the Enforcement Decision Panel and Enforcement Committees are compatible with GEMA's current Rules of Procedure, and how they fit with the legal conventions on delegation of powers. If deterrence is effective (and we think that recent decisions will have caused companies to focus much more strongly

on compliance), there may not be sufficient workflow to justify a separate permanent staff to decide enforcement cases.

- We welcome the proposal to create a small Enforcement Decision Secretariat. It may also be useful to consider a separate function to support the whole investigation process (including any informal dialogue that might simplify the investigation or lead to settlement) so that there is a clear process for considering any procedural questions and gaining updates on progress.
- We would suggest that further consideration needs to be given to the procedural rules around settlements, in particular, whether it is desirable that settlement decisions have to be subject to consultation after they have been agreed. This creates an asymmetry between the company that has agreed the settlement and Ofgem which, at least in formal terms, could walk away. We would encourage Ofgem to explore (in discussion with Government if necessary) whether there are ways to resolve this.
- Publicity is often covered in enforcement frameworks - for example the Regulatory Decision Committee (RDC) makes enforcement decisions on behalf of the Financial Conduct Authority (FCA), and is responsible for issuing and approving decision notices. This helps to ensure that publicity concerning a case is independent and objective. We believe Ofgem should set out policy and procedures governing publicity as part of the review.

Finally, we think Ofgem may wish to review its policy on publicity given at the start of investigations. In some cases, strong publicity risks setting expectations about the outcome of the investigation which may not be borne out by the evidence ultimately revealed. We think a more cautious approach may work better for Ofgem and licensees alike.

If you have any questions regarding any aspect of this response please do not hesitate to contact me.

Yours sincerely,

A handwritten signature in blue ink that reads "Rupert Steele". The signature is written in a cursive style with a long horizontal line extending from the end of the name.

**Rupert Steele**  
Director of Regulation

**REVIEW OF OFGEM'S ENFORCEMENT ACTIVITIES – CONSULTATION ON  
STRATEGIC VISION, OBJECTIVES AND DECISION MAKERS – RESPONSE BY  
SCOTTISH POWER**

**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.**

We think that the proposed vision for enforcement is broadly appropriate but we think it should be adjusted to read "to achieve a culture where businesses put *their duties to* energy consumers first and act in line with their obligations". Some aspects of putting consumers first (such as charging low prices or giving excellent customer service) are matters for competition, not enforcement

This change would also resolve the issue that there may sometimes be a tension between putting consumers' interests first and fulfilling regulatory obligations. For example, it may be the case that meeting a particular customer's needs, e.g. on a network connection, would be incompatible with an obligation to treatment customers in a non-discriminatory way. Similar tensions could arise in respect of the new Standards of Conduct obligations on suppliers.

The enforcement framework should be capable of accommodating any such tensions.

**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.**

Ofgem's proposed strategic objectives are to:

- Deliver credible deterrence across the range of our functions.
- Ensure visible and meaningful consequences for businesses who fail consumers and do not comply.
- Achieve the greatest positive impact by targeting enforcement resources and powers.

Although these are all appropriate objectives for an enforcement regime, we have two points of concern regarding the balance:

- a) The objectives are focused narrowly on enforcement after a suspected contravention has occurred. We think the over-arching objective should be to sustain compliance by licensees. One way to achieve this is through deterrence and sanctions, but an equally important approach (for which there are good precedents in Ofgem's existing practice) is to engage with licensees to assist their understanding and delivery of compliance<sup>1</sup>. The two approaches are not mutually exclusive and we would expect to see both reflected in Ofgem's strategic objectives. We suggest that Ofgem adds a fourth objective along the lines of "Achieve sustained compliance by licensees through education and constructive engagement."
- b) Although a tough deterrence regime may well be consistent with Ofgem's objective of protecting the interests of consumers, it is also important for consumers that there is a

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<sup>1</sup> This is increasingly important with the introduction of principles-based regulation and with the growing complexity of licence conditions (such as those implementing the RMR).

dynamic and competitive market with new entrants challenging incumbents. We think it is important for investor confidence that the enforcement regime is seen to operate fairly and efficiently, particularly given the increasing scope of licence conditions and Ofgem powers. This is likely to be a particular concern for the owners of existing customer facing brands. While robust action should be pursued where necessary, high profile enforcement cases can also have a negative impact on consumer confidence. We would therefore suggest an additional objective along the lines of “Promote confidence in fair and efficient enforcement decision making”. It might also be useful to replace “positive impact” in the third strategic objective with some such phrase as “improvement in compliance” to avoid any suggestion that media profile of enforcement is being sought for its own sake.

Ofgem’s proposed approaches for achieving the strategic objectives are by:

- using a range of enforcement tools – e.g. warning letters, reputational measures, penalties and consumer redress
- identifying poor behaviour early and taking action
- being transparent and fair in enforcement processes and visible in actions taken
- learning from everything we do

In line with our comments on constructive engagement above, we would suggest that the last point should be expanded to include learning across the industry, in particular sharing best practice so that all licensees can achieve compliance in the most efficient and effective manner. Ofgem has used this approach to good effect in some the schemes administered by Ofgem E-serve, where there is regular two-way dialogue between licensees and the relevant Ofgem teams. It would be to the advantage of customers, companies and Ofgem itself if there were a better understanding of behaviour likely to trigger investigations and potential penalties so that the formal enforcement process can be avoided.

Ofgem is proposing to set and review strategic enforcement priorities on annual basis and we think this is a positive development. Publishing and consulting on the priorities would be helpful to licensees and allow other stakeholders such as consumer interest groups, to influence Ofgem’s priorities. This would help improve wider confidence in market and industry arrangements.

We assume that the priorities taken together with the objective to “achieve the greatest positive impact by targeting enforcement resources and powers<sup>2</sup>” mean that Ofgem would be following a risk-based approach to enforcement. This would be in line with other regulators e.g. the Financial Conduct Authority (FCA). It would be helpful for Ofgem to provide further detail on any risk based approach it is following and share it with the industry so that licensees can ensure they are tackling areas of the most concern to consumers, as part of their approach to overall compliance.

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

See comments in response to Question 2 above.

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<sup>2</sup> As currently stated – see discussion above

**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.**

Ofgem's stated aim is to achieve "visibly objective decision making and oversight" which we support. We believe the proposed bodies, ad hoc Enforcement Committees, the Enforcement Decision Panel and the Settlement Committee, would help deliver this objective, subject to the following points.

Enforcement Decision Panel and Enforcement Committees

Ofgem is proposing that the Authority would delegate its powers to decide on contraventions and impose financial penalties to ad hoc Enforcement Committees, drawn from a panel of specialists (the Enforcement Decision Panel) to be recruited by Ofgem and appointed by the chair of that panel. Exercise of these powers is a reserved matter under GEMA's Rules of Procedure<sup>3</sup>, and it is not clear to us that Ofgem's proposal is compatible with these Rules. Paragraphs 17-18 of the Rules permit the Authority to establish a committee and delegate reserved matters to it, but paragraph 19 states that any such committee must have a non-executive member of the Authority as its chairman and that the chairman must appoint the other members of the committee (who, unless the Authority otherwise agrees, must comprise a majority of non-executive members of the Authority). It would therefore appear that, as a minimum, the ad hoc Enforcement Committees would need to be chaired by a non executive member of the Authority, who would then appoint other members of the Committee from members of the Enforcement Decision Panel. It may be the intention that GEMA will amend its Rules of Procedure to permit the proposed level of delegation, but such delegation would still need to be done in accordance with general principles of administrative law, which places limits on the delegation of powers in the absence of statutory authority.

Assuming that the necessary level of delegation can be achieved, it would be helpful for Ofgem to provide greater clarity about the interactions between these bodies, the Authority and other relevant parties including:

- How would members of the Enforcement Decision Panel be selected? Will they be full time employees of Ofgem or part-time appointments who are called on as and when required? (We would favour the latter.) Would there be a register of interests of Panel members to prevent conflicts of interest arising on Enforcement Committees? What guarantees are proposed to underpin independence, eg in terms of security of tenure?
- What are the criteria for constituting an Enforcement Committee? (We would suggest there should be technical expertise pertinent to the case and at least one member should have legal expertise in decision making/contested proceedings.)
- Does Ofgem envisage that the Enforcement Decision Panel would draft and devise its own rules of procedure for Enforcement Committees? How independent in this context will the Panel be?
- How would licensees interact with the Enforcement Committee? Would licensees be able to submit evidence? Would they have the ability to make written and oral representations?

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<sup>3</sup> Item 19 in the Schedule to  
<http://www.ofgem.gov.uk/About%20us/Documents1/Ofgem%20Rules%20of%20Procedure.pdf>

- If deterrence is effective (and we think that recent decisions will have caused companies to focus much more strongly on compliance), what kind of level of workflow is envisaged for the Enforcement Decision Panel?

More generally there is a need to define the roles and responsibilities of these proposed bodies as well as existing bodies such as the monitoring and investigation teams; this is feature of enforcement frameworks in other sectors.

Ofgem is proposing that Enforcement Committees would be required to have regard to Ofgem's annual Strategic Priorities. We are concerned that this may be blurring the purpose of the Strategic Priorities. In our view the Strategic Priorities are most relevant in focusing the activities of Ofgem's enforcement staff during the pre-investigation activities and in deciding whether to open investigations. Once an investigation has been opened and a statement of case referred to the Enforcement Committee, we think the Enforcement Committee should be guided solely by the merits of the case and considerations of proportionality. The severity of any financial penalty should be based on the objective criteria set out in Ofgem's statement of policy on financial penalties and should not be influenced by what Ofgem has selected as a strategic priority.

#### Enforcement Decision Secretariat

We welcome the proposal to create an Enforcement Decision Secretariat and its role in advising Enforcement Committees on procedural rules and issues. In this context, careful consideration will need to be given to the qualifications required for members of the Secretariat. This body will be advising on legal issues as well as, it would appear, making decisions on procedural matters. Procedural issues can often be very important in practice and it may not be appropriate to be hiving these off to a body that is separate from the relevant Enforcement Committee; issues concerning the procedure to be adopted in a case (witness statements, experts, document disclosure etc) are matters that require a good understanding of both the substance of the particular case and of the law, and would be most appropriately dealt with by way of interlocutory application to the decision making body itself.

It might also be worth considering an arrangement whereby that the chairman of the Enforcement Decision Panel is tasked with playing a 'standing' role in order to deal with procedural issues that licensees wish to raise during the course of investigations / enforcement cases and which might not be able to be dealt with by the ad hoc committees.

There is also a case for creating or identifying a separate function to provide procedural support through the whole investigation process (including any informal dialogue that might simplify the investigation or lead to settlement). One of the weaknesses of Ofgem's current enforcement process is the lack of communication with parties to an investigation - and a valuable role for the secretariat would be to ensure that parties are given regular updates on progress and timescales from the outset of an investigation. The procedural role of the secretariat is also important: as well as it should help ensure that procedural best practice is observed by investigation teams.

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

We think the proposals for settlement decision making bodies are broadly sensible, namely a subcommittee of the Authority for 'major' settlement decisions and delegated authority to the Senior Partner (advised by a board of Ofgem Partners – the 'Enforcement Oversight Board') for 'minor' decisions below a specified financial threshold.

However, as a detailed point, we wonder whether it might be clearer to rename the 'Enforcement Oversight Board' the 'Settlement Oversight Board' since its role, as we understand it, would be limited to advising the Senior Partner on settlement decisions below the relevant financial threshold.

We would also suggest that further consideration needs to be given to the procedural rules around settlements. In particular, we would question whether it is desirable that settlement decisions have to be subject to consultation after they have been agreed. From the licensee's perspective, the prospect that, having entered into an agreement in good faith, the agreement may subsequently be overturned could be an impediment. We would encourage Ofgem to explore (in discussion with Government if necessary) whether there are ways to resolve this.

Finally, it would be helpful to clarify the relationship between the Authority and the 'Enforcement Oversight Board'. The consultation suggests that the Authority would have a role in providing high level guidance, to provide direction and promote consistency. However it is unclear whether this guidance would be confined to publication of guidance and policy, and what procedures would be put in place to ensure that the Authority does not influence live cases (given that is the intention).

**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.**

Ofgem proposes that the Authority would retain strategic oversight over all enforcement decisions and would be responsible for producing and reviewing guidance for decision making. We broadly agree with this approach.

The consultation also proposes that the Authority would review enforcement decisions and case progress on an annual basis, and would not seek to influence 'live' decisions. We understand from this that the Authority would respect the independence of the Enforcement Committees and would not be permitted to override their decisions – which we would support. However it would be helpful for Ofgem to clarify if there could be any exceptions to this principle, for example where the Authority considered that a decision has not been made in accordance with the guidance or strategic objectives and principles.

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

Publicity is often covered in enforcement frameworks - for example the Regulatory Decision Committee (RDC) makes enforcement decisions on behalf of the Financial Conduct Authority (FCA), and is responsible for issuing and approving decision notices. This helps to ensure that publicity concerning a case is independent and objective. We believe Ofgem should set out policy and procedures governing publicity as part of the review.

We also believe there is a need to define the roles and responsibilities of monitoring and investigating teams. This would provide greater visibility to licensees of how and why they are being investigated. A good example is the scoping discussions that take place on FCA enforcement cases whereby the investigator and business jointly clarify the scope of the investigation and how it will proceed. A further safeguard in FCA investigations is an independent internal legal review of all investigation cases.

ScottishPower  
29 May 2013