



Making a positive difference
for energy consumers

All regulated persons¹ including suppliers, network companies, generators, shippers, the DCC, consumers and their representatives and other interested parties

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Dear stakeholders,

Open letter on regulatory compliance

This letter sets out our position on regulatory compliance, the roles and responsibilities of different parties, and how our approaches to compliance and enforcement activities interact with one another. It proposes a number of principles to clarify and guide our approach to regulatory compliance. We welcome views on this.

Our aim is to make a positive difference for energy consumers. This underpins all aspects of our work, whether this is through the development of policy, the drafting of licence conditions or other obligations, or engagement with stakeholders. Where regulation is required, we strive to develop proportionate obligations that protect consumers and are clear and attainable for the companies that we regulate. The extent to which we consult with a wide range of stakeholders when developing new policy demonstrates our commitment to developing regulatory practice that is fair, inclusive and focused on outcomes.

We continue to look for ways to become more efficient and effective in how we work and have recently taken the opportunity to review how we engage with stakeholders on regulatory compliance.

Our work on the Enforcement Review (a programme to maximise the impact and efficiency of our enforcement work) and responses to our Forward Work Programme (2014-15) consultation has generated feedback on regulatory compliance from several stakeholders. Ultimately compliance is a responsibility of regulated businesses' boards, but we aim to find ways of supporting this, for example through the provision of information or by clarifying regulatory policy.

Context

The regulatory landscape has evolved over a number of years to encompass the framework of primary and secondary legislation, licences, codes and agreements that exists today. In some areas this has produced a more substantial set of requirements, for example

government initiatives to help increase energy efficiency in households. In other areas regulation has been stripped away, such as the removal of the supply price controls. Regulation has also evolved to reflect more effectively the challenges and opportunities ahead, for example, the move from RPI-X to RIIO for energy network regulation.

The format and style of regulation has also changed. Traditionally licences have been drafted to reflect both prescriptive rules such as “within 2 working days”, and less prescriptive requirements such as “where reasonably practicable”.

However, the use of principles-based regulation, such as the Standards of Conduct (SOC) in the retail market, requires a focus on outcomes. Companies have discretion to find the most effective way for their organisation to achieve the desired regulatory outcome to protect consumers. To encourage compliance with the SOC, we are aiming to enhance our monitoring, engage with suppliers and where relevant share insight to create positive outcomes for consumers.

More recently, the changing regulatory landscape has presented new challenges and opportunities for us to use our resources as proportionately and effectively as possible. For example, a new licensable activity has recently been established to regulate the Data and Communications Company (DCC), a key element of the government’s approach to rolling out smart meters across Great Britain.

Our range of enforcement functions is also increasing. New powers, such as European Union regulation on wholesale energy market integrity and transparency (‘REMIT’), have come into force. A new enforcement power has also been introduced, enabling us to require energy companies that breach licence conditions or other relevant regulatory requirements to provide redress to consumers who suffer detriment as a result.

Compliance principles

Against this changing landscape, we believe that a shared understanding of our approach to regulatory compliance is important, particularly in setting out expectations and responsibilities. To provide this, we have developed five principles to guide our approach to regulatory compliance, on which we would welcome views. These principles apply across all of our work, and to all types of licence holder and regulated person.¹

Principle 1 - Responsibility for regulatory compliance. Responsibility for regulatory compliance rests entirely with the boards of directors of the companies that we regulate.²

They are accountable to energy consumers, the users of their products and services, their shareholders and to us for ensuring that compliance is achieved and sustained through their people, systems and processes. They also need to ensure that information is accurately collected and reported to stakeholders and to us where relevant.

Principle 2 - Clarity of regulatory requirements. Our role is to ensure that regulatory obligations are clear.

We will use a variety of approaches to provide clarity of regulatory requirements for the companies that we regulate. These include:

- engaging in early dialogue when policy is new or complex
- providing guidance or further information on specific areas
- being open and transparent in our decision making
- being accessible to our stakeholders.

Principle 3 - Effective allocation of regulatory resource. We will adopt a proportionate, risk-based and cost-effective approach to the allocation of regulatory resource.

We will focus our compliance activity to ensure that companies remedy potential issues in the most effective and timely manner so as to provide the greatest overall benefit to consumers and the market.³

Principle 4 - Use of appropriate incentives and interventions to secure compliance. We will adapt our approach and the regulatory interventions that we choose to make to secure compliance, including where appropriate by launching an enforcement investigation.

This approach recognises that issues may differ in urgency, complexity, potential consumer or market detriment and between different types of regulated person.

Principle 5 - Working in collaboration with others. Where appropriate we will share information with specific agencies and stakeholders and establish partnerships with other regulators, enforcement bodies and consumer organisations to exchange relevant information on potential compliance issues.

Roles and responsibilities

We undertake a variety of activities to make it easier for companies to meet their regulatory obligations. In some areas we seek to provide greater clarity over terminology, explain obligations in more detail or consider how regulatory requirements apply to new circumstances. We use different tools depending on the situation and the objective we are trying to achieve. Tools can include:

- written guidance
- open letters
- stakeholder workshops
- sharing best practice
- site visits
- use of independent auditors
- enhanced director sign-off requirements
- engagement with chief executive officers
- targeted reporting from companies
- corrective actions plans.

On some occasions this work may require direct engagement with an individual company regarding its particular situation and so may not be apparent to other stakeholders. On others it may involve more generic activity, as illustrated by the examples in Table 1.

Table 1: Examples of Ofgem actions to aid compliance

OBJECTIVE	AREA	ACTIVITY
Build knowledge and skills	Debt and disconnection	Small supplier workshop held in partnership with debt charities to discuss best practice in assessing 'Ability to Pay' and avoiding consumer disconnection.
Explain application of existing rules to new circumstances	Collective switching	Open letter ⁴ clarifying Standard Licence Condition (SLC) 25 - which regulates face-to-face and telephone marketing and sales with domestic customers by suppliers and their representatives - as it applies to Third Party Intermediary (TPI) activities.
Clarify meaning of terms	Retail Standards of Conduct (SOC)	Guidance ⁵ on terminology used within the SOC licence condition to provide clarity regarding how some of the terminology used should be interpreted.
Set out factors indicating compliance	Advanced metering roll-out to larger non-domestic consumers	Open letter ⁶ setting out a non-exhaustive list of factors we may consider when deciding whether a supplier has met the advanced meter obligation.
Explain obligations	Energy Company Obligation (ECO)	Guidance ⁷ to outline which energy suppliers are obligated under the ECO scheme, how they can meet their obligations, when and what they need to report, information on ECO recommended measures.
Explain obligations	RIIO-ED1 environmental report	Consultation ⁸ on an Environment Report Guidance Document (ERGD) to assist DNOs with the scope and contents of their Annual Environment Report under SLC 47.
Clarify meaning and scope of terms	Retail price change notifications	Guidance ⁹ on the meaning and scope of SLC 23 which relates to unilateral variations to Domestic Supply Contracts
Ensure the standardisation of reporting which enables us to collect data from network licensees during the price control period	Reporting of costs, revenues and outputs	Guidance ¹⁰ on the information to be reported annually by Network Operators, to account for their performance under the price control. We collect data to enable us to administer the Special Conditions of the Licensees (the conditions which relate to the price control) which include monitoring the performance of Licensees against price control incentives, monitoring compliance with price control obligations and to enable analysis between price controls and at the subsequent price control review.

We expect companies to take ownership of compliance. We do not believe that our role is to operate in an advisory function in the way that some stakeholders may prefer. In particular, we have noted that some licensees have invited us to review their systems or processes to assess or advise on compliance. On other occasions we have been asked to engage in discussions on very specific compliance points to provide licensees with assurance or informal approval of their particular interpretation of a regulatory requirement. We believe that such an approach could undermine the need for every company operating in a regulated environment to take responsibility for its own culture, systems and actions. This is a key message and consistent with Principle 1.

We recognise that we can still provide valuable assistance to companies in a number of ways, which might include:

- discussing and being clear on the intention of the original policy
- suggesting examples of things we might expect companies to consider in relation to the regulatory requirements in question
- highlighting other relevant information (eg enforcement cases, open letters, guidance, related policy, consumer complaints, stakeholder concerns)
- recognising where emphasis is clear from the drafting of the requirement and where definitions have been provided
- responding to calls for additional guidance, where appropriate.

Compliance and enforcement

It is important to recognise that compliance is related to but separate from enforcement. Our published vision for enforcement is to achieve a culture where businesses put energy consumers first and act in line with their obligations. We have adopted three strategic objectives for our enforcement work¹¹:

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

Providing credible deterrence is central to our enforcement regime. While compliance has a role to play in many situations, it would be inappropriate for us to focus solely on assisting companies to become or remain compliant. Compliance activity can help companies maintain compliance or deliver corrective action to ensure regulatory obligations are met. Enforcement is necessary to deliver corrective action, and importantly also to deter future non-compliant behavior. This deterrent effect can apply to individual organisations and across the industry as a whole.

If enforcement action is ultimately undertaken, distinct compliance monitoring can also play an important role in ensuring that agreed undertakings or assurances from the company in question are appropriately complied with (eg paying compensation to affected consumers or ceasing the infringing behaviour).

New entrants

New entrants, whether in a competitive or monopoly part of the energy market, have to gain a licence from Ofgem. Achieving this is not an endorsement by us of the applicant, its financial status or its business plan, and the licensing framework is not a guarantee of quality for the products and services provided. Rather, the licence is an agreement through which the licensee accepts responsibilities to meet a number of regulatory requirements, and to face the risk of sanctions for failing to do so.


In the retail energy market, it is in the consumers' interest for new entrants to deliver new and engaging business models and innovate in products and prices, in turn enhancing competitive pressure on existing firms to improve service, consumer engagement and behaviour. However, in some instances new market entrants may be less aware of, or equipped to deal with, the regulatory requirements placed upon them.

We are considering how best to provide appropriate information and support to such companies, with one example being the small supplier event referenced in Table 1 which was focused on setting out regulatory obligations on domestic consumer debt and disconnection. In the coming months we will host a further small supplier workshop, in conjunction with Consumer Futures, to discuss how we expect consumer complaints to be handled.

We are open to greater engagement with stakeholders on the issue of compliance and we have and will continue to actively consider what more we may need to do as an organisation to support this.

If you have any questions or views about the contents of this letter, please email Stephanie Tobyn (stephanie.tobyn@ofgem.gov.uk) or call Stephanie on 0141 341 3950.

Yours faithfully



Sarah Harrison
Senior Partner, Sustainable Development

¹ A "regulated person" is defined in section 28(8) of the Gas Act and section 25(8) of the Electricity Act. It includes licence holders, the owner of a storage facility and supply exemption holders.

² This applies equally irrespective of the type of licence, the form of regulatory obligation and the nature of the company (e.g. small scale new entrant or established firm).

³ This can include taking enforcement action where the circumstances suggest that this is required.

⁴ <https://www.ofgem.gov.uk/ofgem-publications/38441/20121009marketing-energy-supply-domestic-customers-third-party-intermediaries.pdf>

⁵ <https://www.ofgem.gov.uk/ofgem-publications/84946/implementation-domestic-standards-conduct-decision-make-licence-modifications.pdf>

⁶ <https://www.ofgem.gov.uk/ofgem-publications/41832/20130228the-roll-out-advanced-meters-larger-non-domestic-consumers.pdf>

⁷ <https://www.ofgem.gov.uk/ofgem-publications/75775/energycompaniesobligationecoguidanceforsuppliers-version11.pdf>

⁸ <https://www.ofgem.gov.uk/ofgem-publications/86483/consultationergd.pdf>

⁹ <https://www.ofgem.gov.uk/ofgem-publications/39266/guidance-letter-slc-23.pdf>

¹⁰ <https://www.ofgem.gov.uk/ofgem-publications/86515/riiot1electricitytransmissionriqsversion1.3.pdf>

¹¹ https://www.ofgem.gov.uk/sites/default/files/docs/decisions/131119_published_version_consultation_decision.pdf