

Notice of decision to impose a financial penalty pursuant to section 27A(5) of the Electricity Act 1989

Decision of the Gas and Electricity Markets Authority to impose a financial penalty, following an investigation into compliance by npower Limited, npower Northern Limited, npower Direct Limited, Electricity Plus Supply Limited¹ and npower Yorkshire Limited (collectively "npower") with reporting requirements under the Renewables Obligation and Feed-in Tariff scheme

27 June 2014

1 Summary

- 1.1 The Gas and Electricity Markets Authority ("the Authority") has imposed a financial penalty on npower Limited, npower Northern Limited, npower Direct Limited, and npower Yorkshire Limited (collectively "npower") following an investigation into npower's failure to report accurate supply data under the Renewables Obligation ("the RO") for England & Wales, and Scotland, and the Feed-in Tariff scheme ("FiTs"), for Great Britain as set out in legislation².
- 1.2 For the RO, by 1 July each year, electricity suppliers are required to inform the Authority of the amount of electricity supplied to customers in England & Wales, and Scotland, during the previous obligation period (from 1 April to 31 March). For the FiTs, this is required by 1 August each year.
- 1.3 Ofgem's investigation concerned npower's reporting of electricity supply data for the obligation periods 2010-2011 and 2011-2012.
- 1.4 The Authority found that:
 - npower underreported the amount of electricity it supplied to customers in England & Wales, and Scotland for the obligation period 2010-2011 and 2011-2012 by 0.08% and 0.28% of its total supply respectively; and
 - as a result other market participants suffered a loss of £162,000 for 2010-2011 and £680,000 for 2011-12 in respect of the RO and £1,600 for 2010-2011 and £61,500 for 2011-12 in respect of the FiTs over the two year period through having had to make higher

¹ On 20 December 2013, Npower Limited completed the sale of Electricity Plus Supply Limited to Telecom Plus plc. The licensee was part of the investigation that the Authority opened on 9 September 2013. However, as explained in footnote 3, the Authority has considered Electricity Plus Supply Limited separately when deciding on the imposition of a penalty.

² The Renewables Obligation Order 2009, the Renewables Obligation (Scotland) Order 2009, Feed-in Tariffs (Specified Maximum Capacity and Functions) Order 2010.

payments than they would otherwise have had to make had npower reported its supply data accurately.

- 1.5 npower took appropriate action to address any market impact caused by the error through retiring ROCs for the 2012-13 RO period and will make a corrective payment into the FITs levelisation fund. npower has also demonstrated to Ofgem that it has made appropriate changes to its internal procedures and controls to mitigate the risk of inaccurate reporting in the future.
- 1.6 The Authority considered it appropriate to impose a financial penalty on npower. In deciding on the level of penalty, the Authority took into account:
 - npower self-reporting the error;
 - the action taken by npower to address the harm suffered by other market participants; and
 - npower's cooperation with Ofgem's investigation, including its agreement to settle with Ofgem.

The penalty is a lower figure than would have been the case if npower had not taken the above steps.

- 1.7 On 19 May 2014, the Authority gave notice under section 27A(3) of the Electricity Act 1989 (the "Act") of its proposal to impose a penalty of £125,000 on npower Limited, npower Northern Limited, npower Direct Limited and npower Yorkshire Limited³ in respect of contraventions of the relevant requirements in the obligation period 2010-11 and 2011-12.
- 1.8 No representations were received in response to the Authority's proposal to impose a penalty of £125,000. The Authority has confirmed the penalty of £125,000.
- 1.9 The penalty must be paid by Monday 11 August 2014.

2. Background

- 2.1. The RO requires licensed UK electricity suppliers to source a specified proportion of the electricity they provide to customers from eligible renewable sources. This proportion increases from year to year and reached 11.1 and 12.4 per 100 Megawatt-hour (MWh) of electricity

³ The Npower group controlled Electricity Plus Supply Limited at the time of the breach and the commencement of the investigation, but has since divested this business. The Authority has decided not to impose a penalty in connection with Electricity Plus Supply Limited and, considering the matter in the round, has imposed the penalty on the four remaining npower licensees mentioned. However, the Authority emphasises that this decision was on the particular circumstances of this case, and should not be taken as an indication of its general approach to cases where divestments, mergers or acquisitions have taken place during the course of an investigation, or of the approach it may take to any such case in the future.

supplied in England & Wales, and Scotland, for the obligation periods 2010-2011 and 2011-2012⁴ respectively.

- 2.2. An electricity supplier can meet its obligations under the RO by:
- presenting the requisite number of Renewable Obligation Certificates (“ROCs”)⁵ to the Authority for each obligation period;
 - making a payment into the buy-out fund equivalent to the value of ROCs they are required to present; or
 - using a combination of the two methods, by presenting some ROCs and making a payment into the buy-out fund for any shortfall.
- 2.3. Buy-out payments are received by Ofgem and “recycled”. The recycling mechanism ensures that the buy-out fund is redistributed to suppliers in proportion to the total number of ROCs that each has presented⁶.
- 2.4. The number of ROCs each supplier must present is calculated by reference to each MWh of electricity supplied by them to customers’ premises during the relevant obligation period. A variety of reports are available to suppliers in respect of the electricity supplies that they make. Reports that are prepared on an “uncorrected” basis reflect the electricity supplied by a licence holder, as measured at customers’ meters. Reports prepared on a “corrected” basis, however, are adjusted to take account of suppliers’ shares of system-based adjustments: and so do not reflect the quantities of electricity supplied by them to customers in the same way as “uncorrected” reports. In order to be able to make accurate and correct calculations of each supplier’s RO the Authority, in exercise of a power conferred by the RO Orders⁷, requires that information relating to the amount of electricity supplied by them to customers in England & Wales, and Scotland, is provided by 1 July following the end of each obligation period on an “uncorrected” basis.
- 2.5. Under the FiTs, suppliers are required to provide an incentive to small-scale generators of renewable energy in the form of FiTs payments. The total costs of these FiTs payments are shared across suppliers in proportion to their share of the total amount of electricity that is supplied to customers by all suppliers in Great Britain. Where the total FiTs payments made by an electricity supplier in a year are less than its allocated share it must make a “levelisation payment” to the Authority in respect of the difference. The Authority then redistributes these funds to suppliers whose total FiTs payments in a year exceed their allocated

⁴ As set out in Schedule 1 to the Renewables Obligation Order 2009 and the Renewables Obligation (Scotland) Order 2009 respectively.

⁵ Renewables Obligation Certificates (ROCs) are issued by the Authority to operators of accredited renewable energy generating stations for the eligible renewable electricity they generate. Operators can then trade the ROCs with other parties, including electricity suppliers who purchase the renewable electricity generated by the operators. ROCs are ultimately used by suppliers to demonstrate that they have met their renewables obligation.

⁶ For example, in the 2011-2012 obligation period, the combined total Renewable Obligations for all suppliers across the UK amounted to 48.9 million ROCs. Of that obligation, 91.5% was met by presenting ROCs and the rest by buy-out payments. As a result, Ofgem recycled £164 million to suppliers.

⁷ Article 53(1),(8) ROO 2009, RO(S)O 2009.

shares of the total of all FiTs payments, again by way of a "levelisation payment". In order to be able to make accurate and correct calculations of the amount and type of levelisation payment to be made by suppliers the Authority, in exercise of a power conferred by the relevant Order⁸ and by the standard conditions of the electricity supply licence⁹, requires that reports of the amount of electricity supplied to customers in Great Britain from individual suppliers are provided in respect of each year. Since the total amount of electricity supplied to customers is being assessed, suppliers are required to use the "uncorrected" information mentioned above.

- 2.6. In June 2013, npower reported to Ofgem that it had made errors in the historic supply data reported to the Authority. This report led to concerns that npower might have breached its reporting requirements under the RO and FiTs.
- 2.7. During the course of the investigation¹⁰ Ofgem confirmed that npower underreported the amount of electricity it supplied to customers in England & Wales and Scotland by 0.08% and 0.28% for the reporting periods 2010-11 and 2011-12 respectively. This is estimated to be equivalent to a value of approximately £842,000 regarding the RO and £63,000 regarding the FiTs.
- 2.8. This error arose due to npower using the wrong supply data from Elexon's data flow to meet their reporting obligations with Ofgem, ie npower used "corrected" supply volumes instead of "uncorrected" supply volumes.
- 2.9. npower accepts that the reporting error was caused by a shortcoming in procedures and controls for reporting to Ofgem. npower became aware of the error as a result of an internal review carried out of their end-to-end reporting process.
- 2.10. Regarding the RO, npower has taken appropriate steps to address the harm caused by its failure to comply with the relevant obligations and specifically the additional payments it would have been required to make to discharge its RO in obligation period 2010-11 and 2011-12. In August 2013, npower retired a total of 22,576 ROCs in respect of the obligation period 2012-13, a value of approximately £896,900¹¹ This step addressed the harm caused to market participants (with interest at five points above base rate¹²) as a result of npower's underreporting.
- 2.11. Regarding the FiTs, npower has agreed to make a payment of £63,000 as a late payment reconciliation in order to address the harm caused for the underreporting in 2010-11 and 2011-12. This payment will be taken as

⁸ Article 34(1) FIT Order 2010.

⁹ Condition 33 schedule A part 3 clause 3.1.

¹⁰ Ofgem engaged with npower and interrogated data held by ELEXON to determine the extent of the error and exactly how it occurred. Ofgem also sent npower an information request dated 06 September 2013.

¹¹ The understated amounts are accrued with a 5.5% interest compounded in a yearly basis between 2011 and 2013.

¹² As set by the Bank of England.

part of the 2013-14 end of year Annual Levelisation reconciliation process as described in paragraph 2.5.

- 2.12. npower has taken steps to prevent these errors from reoccurring and ensure it complies with its reporting obligation under the RO and FiT. npower has amended its internal procedures document, so that it now sets out that uncorrected supply volumes should be used. An additional step in their procedures has also been put in place that involves re-verification with its Energy Reconciliation team for review and comment before data volume is forwarded to its Regulation department.
- 2.13. On the evidence before it, the Authority found that npower breached its reporting obligations under s.32J of the Electricity Act 1989, which is a relevant requirement for the purposes of s.25(8) of the Act. npower admitted this breach.

3. The Authority's decision on whether to impose a financial penalty

General background to the Authority's decision to impose a financial penalty

- 3.1. The Authority considered whether a financial penalty is appropriate in accordance with the requirements of the Electricity Act 1989, and its published Statement of Policy with respect to Financial Penalties (October 2003) ("the Policy"). The Authority has imposed a penalty on npower in respect of contraventions in the obligation period 2010-2011 and 2011-12.
- 3.2. The Authority is required to carry out all its functions, including the taking of any decision as to penalty, in the manner which it considers is best calculated to further its principal objective, having regard to its other duties.
- 3.3. In deciding that it is appropriate to impose a financial penalty, the Authority considered all the circumstances of the case including, but not limited to, the specific matters set out in the Policy. These matters are examined in detail below.

Factors tending to make the imposition of a financial penalty more likely than not

Whether the contravention or the failure has damaged the interests of consumers or other market participants

- 3.4. The Authority found that the interests of other market participants were damaged as a result of the reporting error. npower has taken appropriate action to address the harm to other market participants with regards to the RO and will make the appropriate payment regarding the FiTs by 1 October 2014.

Whether imposing a financial penalty is likely to create an incentive to compliance and deter future breaches

- 3.5. Inaccurate reporting of regulatory information, including information used for the administration of the RO and FiTs, by any regulated company, can lead to the expenditure of considerable resources by Ofgem to identify and resolve. Inaccurate reporting has the potential to cause considerable detriment to other market participants and consumers should it go undetected for a significant period of time. It is therefore important that regulated entities are deterred from providing inaccurate reporting and incentivised to put adequate systems, processes and procedures in place to ensure accurate reporting of regulatory information, including information that Ofgem uses for the administration of environmental programmes, such as the RO and FiTs.
- 3.6. The Authority considers that the imposition of penalties in cases where inaccurate reporting comes to light, such as in this case, is likely to have this effect.

Factors tending to make the imposition of a financial penalty less likely than not

If the contravention is trivial in nature

- 3.7. The Authority considered that npower's contraventions of the reporting requirements under the RO and FiTs are not trivial due to the Authority's reliance on accurate regulatory information, including information used for the administration of the RO and FiTs, in order to carry out its statutory functions effectively.

That the principal objective and duties of the Authority preclude the imposition of a penalty

- 3.8. There is nothing in the Authority's principal objective and duties that precludes the imposition of a penalty in this case.

That the breach or possibility of a breach would not have been apparent to a diligent licensee

- 3.9. The Authority considered that a diligent licensee would have put appropriate procedures and controls in place to avoid such inaccurate reporting.

Conclusion

- 3.10. After consideration of all of the above, the Authority considered that it is appropriate to impose a financial penalty in this case.

4. Criteria relevant to the level of financial penalty

- 4.1. In accordance with section 270(1) of the Electricity Act 1989, the Authority may impose a financial penalty of up to 10 per cent of the annual turnover of the relevant licence holder. Annual turnover is defined in an Order

issued by the Secretary of State¹³ as the applicable turnover for the business year preceding the date of this notice. In the business year ending on 31 December 2013, npower had a turnover of £7.2 billion.

- 4.2. In deciding the appropriate level of financial penalty, the Authority considered all the circumstances of the case, including the following specific matters set out in the Policy.

Factors which are first considered when determining the level of penalty

The seriousness of the contravention and failure

- 4.3. The Authority considered that npower's breach of a relevant requirement under the secondary RO legislation, and a relevant condition under FiT, can be qualified as serious. Ofgem relies on accurate information being submitted by licence holders to carry out its statutory functions and administer environmental programmes, including the RO and FiTs, effectively.
- 4.4. If Ofgem was unable to rely on the accuracy of information submitted by licence holders, there is an increased likelihood of inaccuracy in regulatory decision-making and administration of programmes and it would need to devote more resources to monitoring work. This would lead to an increased burden on both Ofgem and licence holders, and higher overall costs of gas and electricity.

The degree of harm or increased cost incurred by customers or other market participants after taking into account any compensation paid

- 4.5. Other market participants were harmed as a result of npower's reporting error and its consequential under-payment into the buy-out fund and FiTs levelisation fund for the 2010-11 and 2011-12 period. However, the Authority is satisfied that npower has taken action to address the harm to other market participants with regard to the RO and will make the appropriate payment regarding the FiTs by 1 October 2014.

The duration of the contravention or failure

- 4.6. The Authority considered that electricity supply data were reported incorrectly for the reporting periods 2010-11 to 2011-12.

The gain (financial or otherwise) made by the licensee

- 4.7. npower received a financial benefit from not buying additional ROCs and/or making appropriate payments to the buy-out fund in relation to the RO. npower also received financial benefit by paying less than it should have into the FiTs levelisation fund. The Authority noted that this financial benefit has been removed following npower taking appropriate action.

¹³ The Electricity and Gas (Determination of Turnover for Penalties) Order 2002.

Factors tending to increase the level of penalty

Repeated contravention or failure or a continuation of failure after being aware of the contravention

- 4.8. There has been no previous finding of breach of the RO and FiTs reporting requirements against npower. The Authority is satisfied that there was no continuation of the contravention after it was identified by npower. npower has demonstrated to Ofgem that it has taken appropriate steps to revise its procedures and controls for RO and FiTs reporting. As with all suppliers, npower's future compliance with the reporting requirements under the RO and FiTs will be assessed as part of Ofgem's general monitoring work and through its annual supplier audit programme.

The involvement of senior management in any contravention or failure

- 4.9. The Authority did not consider that senior management was involved in any deliberate actions in relation to the contravention.

Absence of any evidence of internal mechanisms or procedures intended to prevent contravention or failure

- 4.10. The Authority considered that internal procedures and controls intended to prevent contravention or failure existed, but were insufficient in this case.

The extent of any attempt to conceal the contravention or failure from Ofgem

- 4.11. npower did not attempt to conceal the contravention and self-reported the breach to Ofgem. The Authority encourages companies to self-report potential issues of concern to Ofgem.

Factors tending to decrease the level of penalty

The extent to which the licensee had taken steps to secure compliance either specifically or by maintaining an appropriate compliance policy, with suitable management supervision

- 4.12. npower has taken steps to secure compliance with its reporting requirements under the RO and FiTs: it has amended its internal procedures document, so that it now sets out that uncorrected supply volumes should be used.

Appropriate action by the licensee to remedy the contravention or failure

- 4.13. npower has taken action, and will be taking action, to address the impact on other market participants by:
- retiring a total of 22,576 ROCs in respect of the obligation period 2012-2013; and
 - making a payment into the FiT levelisation fund by 1 October 2014.

Evidence that the contravention or failure was genuinely accidental or inadvertent

4.14. While there is no evidence that the contravention is wilful or the result of a systemic failure, it cannot be regarded as genuinely accidental or inadvertent, as it was within npower's control to have sufficient procedure and controls in place to ensure compliance with the reporting requirements under the RO and FiTs.

Reporting the contravention or failure to Ofgem

4.15. npower self-reported the contravention promptly.

Co-operation with Ofgem's investigation

4.16. npower has co-operated with Ofgem during the settlement process and has provided information, both on a voluntary basis and in response to an informal information request. Because npower decided not to contest Ofgem's findings, Ofgem did not have to spend additional resources on issuing a statement of case and preparing for an oral hearing. The Authority gave weight to npower's willingness, and agreement, to settle the investigation.

5. The Authority's decision

- 5.1. The Authority considered it appropriate to impose a financial penalty on npower Limited, npower Northern Limited, npower Direct Limited and npower Yorkshire Limited of £125,000 in total in respect of the breach it found had occurred of the RO and FiTs, which it considered to be a reasonable figure in all the circumstances of the case. The penalty is a lower figure than would have been imposed if npower:
- had not self-reported;
 - had not taken action to address the harm suffered by other market participants;
 - had not co-operated with Ofgem during the settlement process;
 - had contested Ofgem's findings.
- 5.2. On 19 May 2014, the Authority gave notice under section 27A(3) of the Act of its proposal to impose a penalty of £125,000 on npower Limited, npower Northern Limited, npower Direct Limited and npower Yorkshire Limited in respect of contraventions of the relevant requirements in the obligation period 2010-11 and 2011-12.
- 5.3. No representations were received in response to the Authority's proposal to impose a penalty of £125,000. The Authority has confirmed the penalty of £125,000.
- 5.4. The penalty must be paid by Monday 11 August 2014.

Gas and Electricity Markets Authority

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