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Dear Sarah,

Consultation on revised enforcement guidelines

This is the British Gas response to the above consultation, dated 28 March 2014.

Generally speaking, we believe that Ofgem's proposals, including the structural changes, support the aim of ensuring that the new processes are more transparent, efficient and effective. The forthcoming work on implementation is clearly important in achieving this aim, and we look forward to engaging in forward-looking and open dialogue with Ofgem. To be most effective, the new approach must be:

- fair and proportionate;
- clearly structured to give suppliers certainty of approach;
- consistent across all suppliers, irrespective of size; and
- based on constructive engagement with suppliers

Ofgem has rightly acknowledged the necessary shift away from a focus on ensuring technical compliance with a set of prescriptive rules, to one more appropriate to a principles-based Standards of Conduct ('SOC') regime.

Prioritisation and visibility of enforcement activities

Ofgem's new vision, objectives and annual strategic priorities will provide helpful context for suppliers in terms of enforcement. We see great value in these to:

1. drive fair, independent and objective decisions;
2. promote greater transparency – i.e. to signal when/how enforcement action is likely to be taken, particularly under SOC which can be subjective and open to interpretation;
3. prioritise resources effectively by Ofgem, which should include keeping existing open cases under review against the annual strategic priorities; and
4. drive continuous improvement in regulation and in the enforcement area as a result of the insight gained into current and likely future issues that drive poor consumer outcomes

Given the influence the annual strategic priorities have on the way in which compliance resource is allocated, they should be subject to regular review with licensees.

Decision-making process

We support the appointment (and roles) of the EDP and EOB, the new composition of Settlement Committees and the new penalty threshold of £100k – but would make the following observations:

- For contested cases, it is positive that the EDP is able to take decisions separately from the investigation team and without the influence of personal views. It is important, however, to

guard against the risk of disconnection between the enforcement and policy teams in connected cases.

- The implementation of proposals for settlement should seek to streamline the process as far as possible, including clearly conveying the benefits of early settlement to suppliers as early as possible in the process, for example in terms of reduced timescales or penalties.

Separately, we believe that Ofgem should review the settlement discount scheme to ensure it provides an incentive for early settlement in all cases, including where a nominal penalty has been imposed to maximise the benefits to consumers.

Opening investigations and alternative actions

When enforcement action is being considered, Ofgem should proactively open discussions, preferably face-to-face, with the affected licensees to talk openly about the nature and scale of the issue, as well as options, next steps and timescales.

This dialogue would support Ofgem in prioritising its resource and increasing the likelihood of disproportionately complex and resource intensive investigations, which can be damaging to the reputation of both the licensee and the industry as a whole. As such we strongly support the use of alternative enforcement tools (paragraphs 3.24 and 3.25) as a way of avoiding Ofgem exercising its statutory enforcement powers wherever possible.

It is also positive to note that Ofgem does not propose enforcing where action is already being taken by another regulator for a breach (paragraph 3.42). We would welcome further clarity that this also applies where a suppliers action might breach consumer regulations and a licence condition (e.g. mis-selling – breaches of both CPRs and SLCs). It is inappropriate for suppliers to be penalised twice for effectively the same thing.

We would like to underline our commitment to working closely and collaboratively with Ofgem on this topic and see the suggested regular enforcement conferences (similar to that held on 26 September 2013) as a vital part of that engagement.

Finally, by the time the final enforcement guidelines are published the reference to the Consumer Protection (Distance Selling) Regulations (paragraph 2.43) will be out of date, as is already the reference to Consumer Futures (paragraph 3.13). We assume Ofgem will update the guidelines to take account of new consumer regulation as well as changes to the consumer landscape.

Our detailed responses to Ofgem's specific questions are set out below in the annex to this letter. Please do not hesitate to contact me if you would like to discuss any aspect of this response.

Yours sincerely

Lex Keel
Head of Energy Compliance
British Gas

Annex 1 – detailed responses to Ofgem's questions

1. Do you agree with the proposed changes to our prioritisation criteria?

Yes, we broadly agree with the proposed changes to Ofgem's prioritisation criteria. It is helpful to have greater transparency in respect of what constitutes a priority matter for Ofgem and the reasons why enforcement action may be taken.

We would expect to look to the annual strategic priorities for enforcement set by the Authority for context with regard to the prioritisation criteria. We would also expect them to be aligned to Ofgem's new enforcement vision[1] and its principal objective to protect the interests of consumers and to promote effective competition.

In terms of communication, it would be helpful if rationale for prioritisation is shared to help suppliers identify the reasons why certain issues or licence conditions will be subject to greater focus by the enforcement team. If, as is likely to be the case, changes in the regulatory landscape result in certain issues receiving an increased priority, it is important that this is clearly signalled to suppliers.

We would note that, given the significant investment associated with embedding compliant operating processes and assuring compliance, it is critical that priorities are applied consistently and fairly across all suppliers, including small and medium suppliers.

We also agree with the other range of factors used to decide whether an issue is a priority matter (as set out in paragraph 3.36) but would make the following comments:

- **Harm or potential harm** (to consumers, to Ofgem's ability to regulate effectively and to competition) is a relevant factor in deciding whether an issue is a priority matter. However, care needs to be taken to ensure that this is quantified accurately and consistently using "lessons learned" from previous enforcement cases as a benchmark.

- **Potential harm**, whilst an important factor in deciding whether an issue is a priority matter, should not be used as a measure for setting penalties for enforcement cases.

- **Deterrent effect** is an appropriate consideration for Ofgem with regard to the likely impact of enforcement action. There should, however, be a level playing field for all licensees, irrespective of size, that is proportionate and reflects the seriousness of the breach.

In paragraph 3.37, Ofgem explains that the list of criteria set out for deciding whether to investigate is not exhaustive and it "may consider other factors where relevant." It is important that Ofgem clearly communicates when such factors become relevant (and why) and that these factors are reflected in future guidance where relevant.

For licence holders who are subject to ongoing (or new) enforcement action, it would also be helpful if Ofgem could review whether the rationale for taking (or continuing) action continues to be relevant in the light of current priorities.

2. Is our approach to the range of alternative actions appropriate?

Yes, we agree with Ofgem's approach to the range of alternative actions and see the natural effect of these to be positive in terms of securing the best outcomes for customers and in avoiding the need for enforcement cases wherever possible.

[1] To achieve a culture where businesses put energy consumers first and act in line with their obligations.

Many enforcement cases that Ofgem investigate are highly complex, resource intensive and damaging to the reputation of both the licensee and the industry as a whole. Therefore, as a general principle we strongly support Ofgem using alternative enforcement tools (as set out in paragraphs 3.24 and 3.25) to avoid exercising its statutory enforcement powers. In particular we see great merit in:

- entering into dialogue or correspondence with a Licensee and warning them about potentially harmful or unlawful conduct; and/or
- agreeing a period of reporting by the Licensee, either to ensure that behaviour is not repeated or to show that they have taken effective action to address the issue

Dialogue between Ofgem and licence holders is likely to be most conducive to the speedy resolution of any compliance concerns, especially under SOC which requires a more qualitative principles-based approach. Whilst the precise nature of engagement between Ofgem and the enforcement team will necessarily depend upon the specifics of the issue, we strongly support the principle of open and transparent engagement.

Suppliers are more likely to want to enter into open dialogue with Ofgem over potential / actual licence breaches if they feel that Ofgem will take a proportionate approach to enforcement and look first at other alternatives – particularly for first offences, or where the licensee is taking (or has taken) active steps to resolve the issue.

On this basis, we would fully support interaction with the enforcement team before Ofgem open a case or pursues enforcement action – including site visits. This is particularly important in the case of SOC concerns, where proactive meetings and dialogue can be exceptionally helpful to ensure a common understanding of potentially subjective issues. This could include sharing of relevant contemporaneous documents that show how the supplier has treated consumers fairly and taken their needs into account.
We also believe that enlisting independent auditors can be a useful way of reviewing (and addressing) particular areas of concern to avoid opening a case or pursuing enforcement action. Such action should be taken into account by Ofgem when deciding to open a case or pursue enforcement action in the same way as a Licensee's willingness to enter into voluntary actions is currently.

3. Do you agree with our proposals for making new cases public?

Whilst we believe it is appropriate for Ofgem to publish on its website every case that it opens (and closes) we agree with Ofgem's suggested exclusions concerning REMIT and other situations where publicity could have an adverse effect.

Although probably Ofgem's intent, it is worth noting that publication is not appropriate where a case has not been opened due to the agreement of appropriate alternative actions (as set out in paragraphs 3.24 and 3.25).

When publicising the opening of a case, Ofgem should make it clear that this does not imply that it has made any finding(s) about non-compliance.

Similarly, all cases made public on opening should also be published on closure – particularly if there was no finding of breach or infringement and the reason why, e.g. due to lack of evidence or the grounds of administrative priorities.

Publishing this information will have a positive effect on public confidence in the industry, and provide reassurance that Ofgem is protecting consumers' interests in line with its statutory obligations.

4. Do you agree with the proposed settlement process?

Yes, we do agree with Ofgem's proposed settlement process, including the role and composition of the Settlement Committee. All parties benefit from settlement through the time and resources saved – including consumers via compensation received earlier than would otherwise be the case.

Importantly, the benefits of settlement need to be more clearly articulated when discussing settlement terms than is currently the case. This includes Ofgem providing clearer information at the outset (and during negotiations) on the extent to which the penalty and timescales are likely to be reduced as compared to contested action. Whilst the draft enforcement guidelines are clear on the steps, outcomes and responsibilities at each stage of the enforcement process, they are less clear about how Ofgem will achieve this in practice.

More generally, in respect of other elements of the settlement process:

- In paragraph 5.3, Ofgem explains that to settle a case, a company under investigation must be prepared to admit to the breaches that have occurred. We believe that settlement should not be forfeited as an option if a company under investigation is not in a position to accept a breach in the absence of sufficient evidence.

- Decisions on cases where the penalty amount is below £100k should be taken wherever possible by a Senior Partner, with advice from the Enforcement Oversight Board made up of Partners from across Ofgem (paragraph 6.10). There are clear efficiencies (both in terms of resources and timescales) to be made in doing so.

- We see an important role for the Board in terms of ensuring consistency of decisions across all licensees and areas of Ofgem's enforcement work. To help with this, the Board needs a clear mechanism to discuss and compare enforcement decisions in line with Ofgem's new vision, objectives and annual strategic priorities.

Finally, it is important that there is separation between "without prejudice" negotiations for settlement and a contested case if efforts to reach a settlement are not successful. In particular, it would be inappropriate for any EDP member who has been involved in settlement discussions to be involved in (or hear) the contested case.

5. Do you agree with the proposed settlement windows?

Yes, in principle we do agree with the general proposal of settlement windows, and in particular:

- the incentive they provide in encouraging settlement as early as possible; and
- consistency with Competition Act 1998 cases by adopting the same settlement discounts and windows as the Competition and Markets Authority

The system of early, middle and late settlement windows will also help to ensure that the benefits of using the settlement process are clear from the outset. Full visibility of the discount scheme for early settlement, whereby proactive co-operation should lead to reduced financial penalties in the majority of cases.

For these benefits to be realised, however, companies must be in a position to be able to make an informed settlement decision. It is, therefore, critically important the information and timescales – including the "reasonable period" (paragraph 5.14) – are clear and transparent.

We do not believe that the discount should be applied to just the penalty amount that has been agreed in the settlement. In recent enforcement cases there is a trend of Ofgem setting a nominal penalty to maximise the contributions to consumers – e.g. in the recent E.ON mis-selling case the penalty was confirmed as £1 with a contribution of £12m to directly benefit fuel poverty customers. This is the right outcome for consumers, but means the settlement windows provide no incentive for early settlement. We would appreciate Ofgem's views as to how an appropriate incentive might be achieved without compromising the redress due to consumers.

We will comment on the levels of discount as part of our response to Ofgem's separate consultation on penalties and consumer redress.

6. Do you have any views on how we propose to implement the new decision-making framework?

The proposal to introduce an EDP for contested cases is a positive development, particularly given the composition of the recently announced Panel includes a wider span of expertise than is the case in the assessment of current enforcement action (including greater direct industry experience). However, the process by which members of this panel are recruited is not entirely clear and we would welcome further information on this and the opportunity to comment on the skills and experience of potential members.

Importantly, the EDP's composition needs to be clear, and its responsibilities relative to the Authority unambiguous. The fact that it is able to take decisions separately from the investigation team in contested enforcement cases and on behalf of the Authority is a positive development. We also agree with:

- the types of decisions for Sectoral and Competition cases that the Panel should take (paragraph 6.27); and
- the process by which decisions are made (paragraphs 6.28 to 6.34)

The risk of this structure, however, is that the enforcement and policy teams may become dislocated. This would be unhelpful – particularly at the current time of important policy change with the ongoing implementation of SOC. The EDP terms of reference, which we look forward to reviewing, can prevent this issue occurring by driving the right "customer outcome based" decisions from the EDP in line with Ofgem's new vision, objectives and the annual strategic priorities. The Authority's annual review of the EDP's decisions and issuing of guidance (where appropriate) can also help to avoid this issue.

We note that Ofgem intends that members of the EDP will be appointed to case decision panels, as needed by the panel Chair, to hear and take decisions in individual cases. It would be helpful if Ofgem could clarify how this selection process will operate to ensure that the members of the EDP have the most appropriate skills and experience for the case, and that decisions are robust, consistent and not informed by conflicting priorities or subjective opinions.

In general, Ofgem's proposals should enhance separation between the investigation and decision-making functions and provide greater confidence in the independence of subsequent decisions.

7. Are these proposals an effective way to allow stakeholders visibility of our timetables and performance?

A transparent and well understood enforcement regime is a prerequisite for a stable and properly functioning retail market. The proposed changes are a positive move towards more open dialogue on compliance between Ofgem and Licensees, supported by proportionate and timely enforcement action that is well communicated, understood and predictable.

As highlighted above, it is important that Ofgem provide clarity on timescales for the investigation, key steps in the process, and implications in terms of settlement approaches.

Equally important is sharing of information with the industry on the topic of enforcement, and adoption of a "continuous improvement" approach. Regular scheduled enforcement discussions with the industry, supported by appropriate metrics, will provide continued focus on Ofgem's strategic priorities, and enable "lessons to be learned" from recent enforcement activities.

The guidelines reflect a significant number of changes to the way Ofgem works, including changes to Ofgem's powers and the regulatory landscape. As such, we welcome Ofgem's commitment to have regard to Better Regulation principles of transparency, accountability, proportionality, consistency, targeting regulatory activities only at cases in which action is needed, and to other principles it considers represent best regulatory practice. However, it would be helpful if Ofgem would provide more specific information on how it intends to have regard of these principles in its enforcement approach.