

Andy McFaul
Office of Gas and Electricity Markets
9 Millbank
London
SW1P 3GE

Paul Whittaker
Director, UK Regulation

paul.whittaker@nationalgrid.com
Direct tel +44 (0)1926 653190

www.nationalgrid.com

22nd May 2014

Dear Mr McFaul

Consultation on revised enforcement guidelines

This is the response of National Grid plc to Ofgem's consultation on its revised enforcement guidelines. National Grid owns and operates the high voltage electricity transmission system in England and Wales and, as National Electricity Transmission System Operator (NETSO), operates the Scottish high voltage and offshore transmission system. National Grid also owns and operates the gas transmission system throughout Great Britain and through our low pressure gas distribution business we distribute gas in the heart of England to approximately eleven million offices, schools and homes. National Grid also has interests in Great Britain in gas metering, gas storage, LNG importation, electricity interconnectors and carbon capture and storage.

This response is made on behalf of all National Grid's regulated businesses in Great Britain. In it, we set out our general remarks about the proposed enforcement guidelines and then deal in Appendix A with the specific questions raised by Ofgem's consultation.

Comments on section 1: Introduction

Overall, National Grid welcomes the revised enforcement guidelines and considers that they provide a clearer and more robust framework to support effective enforcement action by Ofgem across the range of its activities. However, we remain concerned that there are some areas in which the clarity, consistency and effectiveness of the guidelines could be improved.

For example, in paragraph 1.9 of the Guidelines, we note the reference to the statutory requirements for the Authority to have regard to the principles of "best regulatory practice". We are, however, still unsure as to how Ofgem seeks to determine what these principles are aside from the other principles specifically listed in the legislation. While we note and support Ofgem's adoption of the five Compliance Principles for Regulatory Compliance in its open letter of 28 March 2014, we would welcome more clarity from Ofgem in this area (albeit recognising that this is a matter that has implications beyond enforcement work): for example, to what extent will Ofgem look to the non-statutory procedures adopted by the CMA and other sectoral regulators in order to seek out best regulator practice and what benchmarking of its activities will it undertake to ensure that it observes standards which are at least as high as those of its peer regulators within Great Britain and internationally.

We also note that Ofgem's strategic objectives still seem to be drafted in a manner that seems negative. It might be better if these were crafted in a manner that even more clearly linked its enforcement activities to its primary duty of protecting the interests of consumers and perhaps incorporated the aims stated in the covering letter of achieving a transparent, consistent and

proportionate approach to enforcement rather than paraphrasing the wording of the Gas and Electricity Acts.

More fundamentally, we are still concerned that the notion of proportionality is missing from Ofgem's methods of achieving its objectives. It would be helpful if this was included in order to give licensees confidence that Ofgem approach enforcement in a proportionate manner, targeting its resources in a way that best achieves its objectives.

We are also concerned that the guidelines make no reference to the economic incentives that (particularly network) licensees are subject to: we consider that Ofgem should at least recognise that some behaviour that does not adequately serve consumers' interests is (and is more effectively) managed through, for example, price control incentives. For example, some behaviour will lead, through the operation of the incentives, to licensees' revenues being significantly lower than they otherwise would have been. Given that the aim of these incentives is to drive the "right" behaviour by licensees, we consider that there should be a higher hurdle for enforcement action where the licensee's behaviour has led to it already being subject to a revenue "hit" as a result of its activities.

We are also concerned that, while Ofgem has indicated that it will explain why it may depart from the guidelines in a particular case, it has not given any indication as to when it might do so: in order to provide confidence and certainty about its approach to enforcement, Ofgem should set out at least the kinds of circumstances it might consider may justify it taking a different approach in a particular case.

Comments on Section 2: Our Enforcement Powers

While we welcome the comment in paragraph 2.15 that it will not make an order where it considers that a breach is trivial, it would be helpful to have some guidance from Ofgem about how it will determine that a breach is trivial. We would also query whether this is likely to be an approach that Ofgem is ever likely to adopt in practice if its prioritisation criteria are applied correctly or if it is using its discretion to close cases under section 7 effectively.

Picking up on our comment above about departure from the procedures set out in the guidelines, we would be keen for Ofgem to outline when it will not follow the flowchart referred to in paragraph 2.18.

Comments on Section 3: Opening a Case

We welcome the comments in paragraph 3.5 that self-reporting will be viewed favourably in determining what action Ofgem will take and determining the amount of any penalty. We consider that this is an essential part of trying to create a culture in which licensees transparently seek to "do the right thing".

As for whistleblowing, while we welcome appropriate guidance for whistleblowers, we consider that, at least in competition law cases, Ofgem should follow the same procedures as are adopted by the CMA to ensure consistency of approach.

We consider that the alternatives that Ofgem has set out in paragraphs 3.24ff to enforcement action are helpful in demonstrating that Ofgem has a range of approaches it may take depending upon the case. We would also welcome clarity as to whether the use of an alternative approach would require the licensee to make an admission of breach. It is also not clear how this approach will interact with the prioritisation criteria for opening a full investigation and guidance on this would be helpful. We also note the obligation to consider the use of competition powers and query whether paragraph 3.22 accurately reflects the approach Ofgem is required to take.

We welcome the clarity provided by the list of prioritisation criteria set out in paragraph 3.36, but consider that it would be helpful if some indication could be given as to whether there is any comparative weighting between the criteria and what that weighting is: for example, does "fit" with the Authority's prioritisation criteria trump all the other criteria? In this light, we are of the view that, given the Authority's primary duties, the most important criterion in determining whether to take action is

whether the matter is likely to have harmed consumers and the potential extent of that harm. We also consider that the level of any financial gain accruing to the company might not, in reality, be a separate element here, but rather a proxy for the potential harm suffered by consumers. Similarly, we consider that “recidivism” (grounds 6) and 7)) appears to be more important than whether the breach is ongoing or not, given that it is in the nature of some breaches that they can only be committed by “one-off” events.

We are concerned that the statements about when the Authority will take action at the same time as another body (paragraph 3.44) does not adequately explain how this might sit with the statement in paragraph 3.42 that the Authority will ensure that a company is not penalised for the same breach twice: in particular, where a single course of action might breach more than one set of rules, it is possible that the same facts could lead to separate breaches – is it the case that the Authority may still consider investigating in these circumstances (which may lead to more than one penalty being imposed in relation to the same set of facts)?

Comments on Section 4 – Conducting Investigations

We welcome Ofgem setting and communicating provisional timelines and updating them as matters develop: we would, however, note that these timescales need to be sufficiently flexible to enable the Authority both to conduct its investigation effectively and to allow the company under investigation sufficient opportunity adequately to respond to the investigation and exercise its rights to a fair opportunity to present its case. In this context, it is also important that, in publishing the opening of a case (paragraph 4.8), the Authority states clearly that this does not imply any finding of breach.

More generally, in this section it would be helpful if greater distinction were made between competition law and sectoral investigations because of the different procedural rules applicable to each. For example, the competition authorities have adopted a particular approach in relation to whistleblowers: the Authority should conduct its activities in relation to whistleblowers in a manner consistent with these rules. In particular, the Authority should consider the impact of publication on the interests of a whistleblower in deciding whether to offer anonymity (see paragraph 4.9).

Ofgem has not addressed (in paragraph 4.19ff) the issue of concurrent information requests which we have raised previously. In any investigation there is often a small number of individuals within the company under investigation (however large) who are able to deal with information requests: the burden on these individuals of dealing with concurrent requests can be very significant therefore challenging the ability to deliver responses within requesting timeframes. In this light, it would be helpful if Ofgem would give commitments:

- to be mindful of companies’ internal resources in setting deadlines for responses (and not just assume that large companies have effectively limitless resources to bring to bear in responding to questions requiring specialist knowledge or the provision of technical data); and
- issue concurrent information requests only in exceptional circumstances.

In this context, we would also welcome some guidance as to what may constitute a “good reason” for requesting an extension of time to respond to an information request (see paragraph 4.24) especially given our comments about companies’ internal resources.

We also note the comment that failure to cooperate with information requests may be considered an aggravating factor in setting fines (see paragraph 4.25): we note that this statement is not entirely consistent with the approach to setting fines in competition law cases set out in the CMA’s guidance as to the appropriate amount of a penalty in competition law cases (which treats this as an aggravating factor only where the breach is persistent and repeated). In any event, we consider that this statement best sits in the Authorities penalties statement, rather than in this Guideline.

Comments on section 5: Contesting a case

We note the requirement that the licensee make an admission of breach to settle a case. This is disappointing as it may reduce the number of settlements that are reached by Ofgem as the licensee who does not consider there has been a breach and will not admit one may nevertheless be incentivised by avoiding further enforcement action. Furthermore, this approach is not consistent with the approach taken in competition law where companies under investigation have the opportunity to conclude cases by offering binding commitments. As such, we consider that the Authority should reconsider this position and seek to tie the settlement process more closely to the procedure for closing a case set out in sections 3.25 and 7 as it is not clear precisely how these approaches will interact.

We note that certain cases may not be appropriate for settlement but Ofgem does not give any indication of the criteria that will be used to make this assessment: further guidance in this area may also be helpful. We are also somewhat confused that cases may not be suitable for settlement where a point of law is at stake (see footnote 114): the Authority has no jurisdiction to determine points of law and, therefore, this approach implies that any finding will be appealed to the Court for determination. The Authority does not have any control over this: would these cases be more suitable for closure under the procedure under paragraph 3.25? Further guidance and clarity in this area would be helpful.

It would be helpful if Ofgem would explain how long it considers a reasonable period is likely to be to keep the early settlement window open so that licensees are aware in advance how long they will have to consider the settlement options and ensure that the appropriate members of senior management are available. Without this clarity, opportunities to settle cases may be lost.

In relation to paragraph 5.19, in addition to the provisions of 6.9, if settlement negotiations fail, all those involved in the settlement process and discussions and review of settlement documents should not be involved at all in any way from then on in respect of the investigation or decision making bodies.

In relation to paragraphs 5.26 to 5.28, we consider that Ofgem should state that its starting point should be full disclosure of documents to the licensee under investigation in order to ensure that their open and transparent approach to enforcement is followed.

We consider that a period of 28 days for the provision of written representations may be too short in some circumstances and that Ofgem should provide some guidance as to the sorts of factors when determining what period is appropriate on a case-by-case basis (for example, complexity, novelty/seriousness and urgency).

We note that the settlement process discounts set out in paragraph 5.49 refer to “early” and “late” settlement windows, but the flowchart in the Appendix for sectoral cases indicates that there is a middle settlement window (see also paragraph 5.28 of the consultation on financial penalties): as such there appears to be an inconsistency in approach – this must be resolved in the final Guidelines.

Comments on section 6: Decision making and appeals

We welcome Ofgem’s commitment in paragraph 6.24 to allow licensees who have agreed a settlement to withdraw from it if it is changed following Ofgem’s statutory consultation on it. However, it is not clear whether such withdrawal could negatively impact upon the future enforcement process and level of penalty. In particular, we consider that, while it is appropriate for a company to leave the settlement procedure in the event that public consultation indicates that the settlement agreed is not appropriate, given that this is a factor beyond the control of the party under investigation, some discount should still be available from the level of financial penalty that would otherwise be applied in a contested case in order to recognise the company’s willingness to settle.

While we welcome the factors that the Panel will consider (and set out at paragraph 6.33), we consider that it would be beneficial for Ofgem to explain what other factors the Panel may consider in addition to the items listed in this paragraph.

Comments on section 7: Closing cases

While we welcome the clarity that Ofgem provides in this section, as indicated above, this section does appear to be something of an “afterthought” in the enforcement process, rather than an integral part of it. As such, we would prefer to see this material more clearly “woven” into the section on the conduct of an investigation and, in particular, the interaction between this material and the comments in paragraph 3.26 about whether a case can be terminated without a finding of breach clarified.

We hope that Ofgem finds these comments helpful in finalising the Enforcement Guidelines. However, if there is anything in our response that you would like to discuss further, please do not hesitate to contact James Wynn Evans (01926 655448, james.wynn-evans@nationalgrid.com) or Charlotte Digby (01926 655229, charlotte.digby@nationalgrid.com).

Yours sincerely

[by e-mail]

Paul Whittaker
Director, UK Regulation

Appendix A – responses to specific questions

Q1 Do you agree with the proposed changes to the prioritisation criteria?

Please see our comments above in relation to section 3 of the guidelines.

Q2 Is our approach to the range of alternative actions appropriate?

We consider that resolution of cases through the use of compliance measures is better than going through a full investigation in suitable cases. We would, however, welcome greater clarity as to how this might fit with the comments in paragraph 3.26 of the Guidelines and the closure of cases pursuant to Section 7.

Q3 Do you agree with our proposals for making new cases public

We note Ofgem's proposed approach to publication. We consider that any publication should make it clear that the commencement of an investigation does not imply that any breach has occurred.

Q4 Do you agree with the proposed settlement process

We welcome the improvements made to the settlement process as part of the consultation. We do, however, have some additional comments on it: please see our comments in relation to section 5 above.

Q5 Do you agree with the proposed settlement windows

We note that the settlement process discounts set out in paragraph 5.49 refer to "early" and "late" settlement windows, but the flowchart in the Appendix for sectoral cases indicates that there is a middle settlement window (see also paragraph 5.28 of the consultation on financial penalties): as such there appears to be an inconsistency in approach – this must be resolved in the final Guidelines.

Q6 Do you have any views on how we propose to implement the new decision making framework?

We consider that the new framework is a good step forwards and a pragmatic approach that is much clearer than what has gone before. The question remains as to when the new Guidelines are effective from (see Para 1.14) and in which circumstances Ofgem may depart from these Guidelines.

Q7 Are these proposals an effective way to allow stakeholders visibility of our timetables and performance

We consider that the proposed process is much more transparent as to why certain process steps will happen and by when: this will benefit regulated entities, Ofgem and consumers.