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23rd June 2014

Response to Ofgem's consultation: financial penalties and consumer redress policy statement

Dear Sarah,

I attach Energy UK's response to the above consultation, which is not confidential.

If you have any questions, please do not hesitate to contact me on 020 7747 2963 or daisy.cross@energy-uk.org.uk.

Yours sincerely

Daisy Cross
Policy and External Relations Executive

Ofgem's financial penalties and consumer redress policy statement

Energy UK response

23 June 2014

1. Introduction

- 1.1. Energy UK is the trade association for the energy industry. We represent over 80 members made up of generators and gas and electricity suppliers of all kinds and sizes as well as other businesses operating in the energy industry. Together our members generate more than 90 per cent of the UK's total electricity output, supplying more than 26 million homes and investing in 2012 more than £11 billion in the British economy.
- 1.2. This is a high-level industry view; Energy UK's members may hold different views on particular issues. We would be happy to discuss any of the points made in further detail with Ofgem or any other interested party if this is considered to be beneficial.

2. Executive summary

- 2.1. Energy UK welcomes the opportunity to respond to Ofgem's consultation as part of its wider review of its enforcement and compliance processes. Energy UK also refers Ofgem to its recent submission to Ofgem's consultation on its draft enforcement guidelines¹ and our paper on regulatory compliance which we sent you on 18th June 2014.
- 2.2. Regarding settlement discounts, Energy UK believes that discounts Ofgem applies should cover any mandated parts of a financial penalty, and also any voluntary payment the company may have already made to remedy the situation to ensure consistency and fairness (the full penalty sum is subject to discount in every case), and that Ofgem has the incentive to settle cases swiftly.
- 2.3. Energy UK strongly agrees with Ofgem's objective to take into account remedial measures already undertaken by the company when determining the amount of a financial penalty.
- 2.4. In line with government's intent behind awarding Ofgem's redress powers, Energy UK urges Ofgem to clarify that it would use these powers as a backstop option, with voluntary agreements arranged by suppliers being the initial aim.
- 2.5. Where cases have been settled without company fault being established, members would like Ofgem's guidelines to allow the settling of cases without a requirement on the company to accept the judgement of breach.
- 2.6. Energy UK wishes to understand whether partial settlement is possible under Ofgem's guidelines, and how it would work in practice.
- 2.7. Ofgem states that discounts will only be applied to the penal element of its fines, rather than to both the penal and redress elements. It should be possible for Ofgem to further reduce any penal element (where both are being proposed) in proportion to what the reduction in the redress element may have been.

¹ <http://www.energy-uk.org.uk/publication/finish/171-consultation-responses-may-2014/1121-energy-uk-response-to-ofgems-consultation-on-draft-enforcement-guidelines-23-may-2014.html>

- 2.8. Regarding suppliers requirement to pay administrative costs, Energy UK seeks clarity from Ofgem as to how costs will be divided fairly where several suppliers are under investigation for the same infringement, or where several suppliers commit the same breach in succession.

3. Responses to individual consultation questions

Objectives and duties in relation to penalties and redress

Q.1 Are these objectives appropriate?

- 3.1. Energy UK is supportive of Ofgem's objectives and duties as set out in the policy statement. Under Ofgem's new rules there is a greater need for transparency to ensure that penalties are derived proportionately and fairly, particularly where Ofgem is calculating penalties for consumer detriments that are intangible and difficult to quantify, such as customer inconvenience. Energy UK strongly agrees with the objective set out in paragraph 2.6 – that the Authority will take into account 'remedial measures' already undertaken by the company when determining the amount of a financial penalty. This is assuming that redress values are included in the definition of 'remedial measures'.
- 3.2. It shouldn't be the case that Ofgem automatically issues Redress Orders to suppliers when a breach is identified. In its 2012 consultation² DECC states it would expect that Ofgem's powers to secure redress 'would generally operate as a backstop for use in those cases where the company in question has failed to address a significant outstanding detriment, and to act as an incentive on companies to offer redress.' Energy UK supports this objective, and calls for Ofgem to clarify its policy statement to reflect its original mandate - that voluntary arrangements should be agreed in the first instance, with enforced redress orders only used in the last resort. Arrangements designed and implemented by a supplier itself will often be more practicable and efficient than arrangements imposed by the regulator.

Determining the amounts payable under penalties and redress orders

Q.2 Is the proposed process for determining the amount of penalties and/or redress appropriate?

- 3.3. Energy UK is supportive of Ofgem's process as outlined in its policy statement. Its members call for Ofgem's transparency around how it levies financial penalties. Ofgem could publish its penal element parameters, for instance in ranges that would apply to various cases.

Q.3 Do you agree with the proposed factors that may aggravate or mitigate the amount of a penalty or redress payment?

- 3.4. With regards to self-reporting of breaches, Energy UK considers that there is a difference between a supplier reporting a previously unknown infraction, and it reporting an incident where it is aware that the announcement of an investigation is imminent (for example where it has been subject to a specific information request). Energy UK urges Ofgem to take into account such differences, perhaps via greater leniency in such cases where companies draw to attention an issue that Ofgem had no previous awareness of.

Settlement discounts

Q.4 Do you agree with the proposed settlement percentage discounts in cases under the Gas Act or Electricity Act?

- 3.5. In its consultation letter on its revised enforcement guidelines³, Ofgem states that it would envisage an early settlement window as usually being '28 days from when we send a company the draft penalty statement and/or consumer redress order.' Energy UK notes that – given the time that it could take to

² https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/42937/4975-consultation-on-a-proposed-new-power-for-ofgem-to-.pdf

³ <https://www.ofgem.gov.uk/ofgem-publications/86884/enforcementreviewguidelinesanddeliverableconsultationletter28march2014.pdf>

compose an accurate picture of some issues raised - this is a short deadline, and urges Ofgem to allow more time for companies to meet this first deadline.

- 3.6. The longer an investigation progresses, the more likely it is to uncover more evidence of breach or lack thereof, and therefore the value of the penalty Ofgem initially foresees increasing or decreasing. In consideration of this, Energy UK wishes Ofgem to confirm whether the penalty value it decides initially is a fixed amount, or whether this amount can increase/decrease as the investigation progresses.
- 3.7. Energy UK understands that the early settlement window is opened when a draft penalty notice and/or redress order and press notice are served. Our members also wish to understand whether this deadline marks the point at which Ofgem has gathered all pertinent data, or whether it marks the point at which Ofgem decides to take action. The answer to this question may influence the penalty value levied, depending on whether this is fixed or variable as discussed in paragraph 3.5.
- 3.8. Energy UK understands that, in the past, some cases have been settled without company fault or breach being established. In its consultation on its draft enforcement guidelines⁴ Ofgem states that 'to settle a case, a company under investigation must be prepared to admit to the breaches that have occurred'. Energy UK would like to see an option retained which allows companies to settle a case without having to accept the judgement that a breach has occurred. This would ensure that the final judgement in such cases reflects the fact that a breach has not been formally established. Could Ofgem, for instance, include settlement without the finding of a breach as a designated alternative action under 3.25 in its draft enforcement guidelines.
- 3.9. Ofgem does not refer to partial settlement - and its treatment of this scenario - in its draft enforcement guidelines or in its policy statement. Partial settlement could occur where more than one breach is levelled against a company, and the company accepts fault on one or several accounts, but not all. Energy UK wishes to understand whether partial settlement is possible under the guidelines, and how this would work in practice (would the proposed settlement windows apply, and how would this circumstance be reflected in the case closure notification, for instance?). Partial settlement could bring cases to a conclusion earlier than if decisions are contested. Therefore, any redress to consumers would be delivered quicker under a partial settlement arrangement.
- 3.10. Ofgem states that discounts will only be applied to the penal element of its fines, rather than to both the penal and redress elements. Energy UK agrees that settlement discounts should not apply to use of the statutory redress power, as this would not fully compensate customers affected, and would therefore fail to reflect fair redress to the appropriate group of customers. However, it should be possible for Ofgem to further reduce any penal element (where both are being proposed) in proportion to what the reduction in the redress element may have been.
- 3.11. Energy UK believes that discounts Ofgem applies should encompass both the mandated parts of a financial penalty, but also any voluntary payment the company may have made already. This would ensure that the full penalty sum is subject to discount in every case (guaranteeing consistency and fairness across all cases), and that Ofgem's intent to incentivise swift settlement is reflected. Energy UK asks Ofgem to clearly state that this is the case in its guidelines.

Requirements that may be set out in a consumer redress order

Q.5 Do you agree with the proposed policy on determining who receives payments where consumer redress powers are used?

- 3.12. Ofgem should ensure that its compensation principles are consistent with the principles of other organisations which make financial awards to consumers, such as Ombudsman Services: Energy and the small claims courts.

⁴ <https://www.ofgem.gov.uk/ofgem-publications/86887/draftenforcementguidelines28march2014.pdf>

Q.6 *Are there any other potential consumer redress requirements that we should specifically refer to in section 7 of the policy statement?*

3.13. Energy UK is satisfied with the requirements currently set out in section 7 of the policy statement.

Treatment of consumer detriment

Q.7 *Do you agree with the proposed approach to the treatment of detriment?*

3.14. Energy UK wishes to understand whether Ofgem means for redress to cover immediate and/or consequential losses, such as insolvency. If it covers consequential losses, members seek clarity as to whether Ofgem will apply limits here, and what these might be.

3.15. Regarding the use of proxy where it is not possible or practicable to pay redress directly to customers affected, Energy UK members urge transparency around how Ofgem will decide an appropriate proxy where redress does not apply to fuel poor groups.

3.16. Energy UK asks Ofgem to define the terms 'loss', 'damage', 'harm' that it uses in its consultation.

Administering consumer redress orders and bearing administrative costs

Q.8 *Should administrative costs be borne by the company in addition to any compensation or other payments that may be required?*

3.17. Members consider that there may be cases where several suppliers could be under investigation for the same infringement. There may also be cases where several suppliers commit the same breach in succession. In this instance, where a central redress scheme (such as a charitable fund) is set up, all fixed administrative costs associated with the redress exercise would be borne by the supplier A, who is reprimanded first and required to set up a redress scheme. Suppliers B, C and D, who are reprimanded after this redress scheme is set up, are subsequently required to offer redress for the same infraction, but would not have to financially contribute to the redress scheme. Supplier B, C and D would benefit from supplier A's initial administrative payout in this case.

3.18. Energy UK wishes to understand Ofgem's process of dividing common administrative costs to all suppliers involved in the scenarios set out in 3.16 to ensure that costs are distributed fairly across all parties.

3.19. Energy UK asks Ofgem to amend its statement to reflect that material administrative costs are netted off the total penalty/redress amount to incentivise Ofgem to come up with manageable redress arrangements.