

Notice of intention to impose a financial penalty pursuant to section 30A(3) of the Gas Act 1986 and section 27A(3) of the Electricity Act 1989

Proposal of the Gas and Electricity Markets Authority ("the Authority") to impose a financial penalty, following an investigation into E.ON Energy Solutions Limited's ("E.ON") compliance with its obligations under standard licence conditions ("SLCs") 23.6 and 24.3 of its Gas and Electricity Supply Licences

2 April 2015

1. Summary

- 1.1. The Authority proposes to impose a financial penalty on E.ON following an investigation into E.ON's compliance with SLCs¹ 23.6 and 24.3 in relation to its January 2013 price increase, and SLC 23.6 in relation to its January 2014 price increase.
- 1.2. SLC 23.6 applies to unilateral disadvantageous variations of contract (including price increases). It provides (among other things) that a supplier must treat a price increase as ineffective and neither enforce nor take advantage of it in respect of certain customers who intend to switch supplier.
- 1.3. SLC 24.3 relates to termination fees. It contains restrictions on the circumstances in which a supplier may include contract terms requiring a domestic customer to pay a termination fee to end the contract. These include where the licensee is required to give a price increase notice under SLC 23.3 (SLC 24.3(c)).
- 1.4. The Authority finds that:
 - In relation to its January 2013 price increase, due to a combination of manual error and limitations in E.ON's systems, a number of credit and prepayment (PPM) customers who gave notice to terminate their contract as a result of the higher price were charged a higher price for the period from the January 2013 price increase (for credit customers) or the date the prices were added to their meter (for PPM customers) up to when those customers left E.ON, and/or were also incorrectly charged a termination fee, in contravention of SLCs 23.6 and 24.3. The Authority finds that between 6,150 and 23,655² customers who notified E.ON of their intention to leave were affected by E.ON's failure to comply with SLC 23.6, and 882 of these customers, were also affected as a result of E.ON's failure to comply with SLC 24.3. Paragraph 3.6 contains further details relating to the numbers of customers affected by the breach of SLC 23.6.

¹ The SLCs referred to in this notice have similar wording in the Gas and Electricity Supply Licences and are interpreted by the Authority in a consistent manner. In this notice, a reference to a SLC by number refers to the identical condition in both licences. All defined terms used in this notice are deemed to have the same meaning as in the SLCs, unless indicated otherwise.

² The actual number affected by SLC 23.6 is unknown but is likely to be significantly less than the upper limit of 23,655 customers.

- In relation to its January 2013 price increase, due to a lack of adequate oversight and monitoring control, a further number of PPM customers (up to 510 customers) who gave notice to terminate their contract as a result of the higher price were also charged the higher price from the date the higher charges were added to their meter until they left E.ON and not refunded in a timely manner, in contravention of SLC 23.6. Information showing that these customers were affected was only provided very late into the investigation.
 - In relation to its January 2014 price increase, due to system errors, a number of credit customers who gave notice to terminate their contract were charged a higher price for the period from the January 2014 price increase up to when those customers left E.ON, in contravention of SLC 23.6. Due to a lack of adequate oversight and monitoring control, a number of PPM customers who gave notice to terminate their contract as a result of the higher price were also charged the higher price from the date the higher charges were added to their meter until they left E.ON and not refunded in timely manner, in contravention of SLC 23.6. Information showing that these customers were affected was only provided very late into the investigation. These credit and PPM customers had not been charged a termination fee so SLC 24.3 was not engaged. The Authority finds that around 16,500 credit customers and around 6,500 PPM customers were affected in total.
- 1.5. E.ON has taken action to improve its compliance with SLCs 23.6 and 24.3. In July 2014, E.ON informed Ofgem that a project team was being set up to undertake an end-to-end review of the system.
 - 1.6. E.ON has agreed to provide evidence that its system and any measures and system fixes are robust with the use of an independent external auditor. E.ON has also agreed to implement any appropriate recommendations made by the auditor relating to non-compliance of SLCs 23.6 and 24.3 prior to any general price increase.
 - 1.7. The Authority has taken into account that E.ON has offered to settle this investigation and to make a payment of £7,750,000 (less £1) in consumer redress; £1,400,000 is in respect of the breaches of SLCs 23.6 and 24.3 in relation to the January 2013 price increase and £6,350,000 is in respect of the breach of SLC 23.6 in relation to the January 2014 price increase.
 - 1.8. This payment of £7,750,000 (less £1) will be made for the benefit of Citizens Advice Energy Best Deal Extra and will be used to provide one-to-one energy advice to vulnerable consumers across Scotland, England and Wales.
 - 1.9. Having considered all the circumstances of the case, the Authority considers this redress payment will be of greater benefit to consumers than if a significant financial penalty were to be imposed.
 - 1.10. In the circumstances, the Authority hereby gives notice under section 27A(3) of the Electricity Act and section 30A(3) of the Gas Act 1986 of its proposal to impose a penalty of £1 on E.ON in respect of the contraventions set out above provided that as at the date of any final penalty notice issued by the Authority pursuant to section 30A(5) of the Gas Act 1986 ("Gas Act") and section 27A(5) of

the Electricity Act 1989 ("Electricity Act") ("Final Penalty Notice"), and at a date to be notified by the Authority, E.ON has paid £7,750,000 (less £1) by way of consumer redress as set out above.

- 1.11. The Authority considers the penalty to be reasonable in all the circumstances of the case. If E.ON had not agreed to settle this investigation by making this redress payment, the Authority would have considered it appropriate to impose a much larger penalty in view of the seriousness of the contraventions.
- 1.12. Any written representations or objections with respect to the proposed penalty must be sent to Andrea Gregory (andrea.gregory@ofgem.gov.uk) by 5pm, 5 May 2015.
- 1.13. The Authority would prefer it if, as far as possible, responses were provided in a form that can be placed on the Ofgem website. Should you wish your response or part of your response to be confidential please indicate this clearly and give reasons for this request. Any such requests will be considered by Ofgem on a case by case basis.

2. Background

The relevant licence Conditions:

- 2.1. The licence conditions relevant in this investigation are SLCs 23.6 and 24.6. Different versions of SLC 23.6 were applicable to the breaches being investigated for the price increase in January 2013 and the price increase in January 2014.
- 2.2. When considering the January 2013 price increase, an earlier version of SLC 23.6, is applicable and, in relation to the January 2014 price increase, the current version of SLC 23.6 is applicable³. The relevant provisions are summarised below:
- 2.3. SLC 23.6 as in place at the time of the January 2013 price increase⁴ required that, among other things, a licensee must treat a unilateral price variation as ineffective and neither enforce it nor take advantage of it where: a) the Domestic Customer notified the licensee after he became aware (by any means) of the variation on or before the date on which the variation had effect that he was ending the Domestic Supply Contract by changing his supplier; and b) no later than 15 Working Days after such notification by the Domestic Customer, the licensee received notice that another supplier would begin to supply the Domestic Customer's premises within a reasonable period of time after the date such notice was given. This meant that where a supplier was notified that a customer wished to terminate their contract no later than 15 working days from the notification of a price rise by the supplier, the supplier was not permitted to apply the higher charges to that customer if they subsequently received notice confirming that another supplier would be taking over supply within a reasonable period of time.

³ The current versions of the SLCs can be found at: <https://www.ofgem.gov.uk/licences-codes-and-standards/licences/licence-conditions>

⁴ Copies of SLC 23.6 applicable to the January 2013 price increase are set out at: <https://epr.ofgem.gov.uk//document/Download/28025>; <https://epr.ofgem.gov.uk//document/Download/28058> <https://epr.ofgem.gov.uk//document/Download/25774>; <https://epr.ofgem.gov.uk//document/Download/28094>

- 2.4. SLC 23.6⁵ as applicable to the January 2014 price increase requires that, among other things, a licensee must treat a price increase as ineffective and neither enforce it nor take advantage of it where: a) no later than 20 Working Days after (but not including) the date on which the price increase has effect, the licensee receives notice that another supplier will begin to supply the Domestic Customer's premises within a reasonable period of time after the date on which such notice was given; and b) another supplier begins to supply the premises within a reasonable period of time after the date on which such notice is given. This means that the supplier is not permitted to apply the higher charges to the customer if they have received notice that another supplier will take over supply to the customer's premises no later than 20 working days after the date of notification of a price rise by the supplier, and such other supplier begins to supply within a reasonable period of time of the notice.⁶
- 2.5. The provisions of SLC 24.3, as applicable at the time of the January 2013 price increase, provided that a licensee may include a term in a Domestic Supply Contract requiring a Domestic Customer to pay a Termination Fee to end that contract except in certain circumstances. Among such circumstances, it included an exception where the licensee gives a price increase notice and the customer notifies the licensee after becoming aware (by any means) of the variation, on or before the date on which the variation has effect, that he was ending his contract by changing his supplier. This means that where a customer gave notice to terminate their contract after notification of a price increase as set out above, the supplier must not require a customer to pay a termination fee.
- 2.6. Ofgem sent E.ON three information requests between May and August 2014 to gather further information regarding the contraventions in relation to both price increases. E.ON provided responses to all information requests as required.

Previous similar case:

- 2.7. In November 2011, E.ON notified Ofgem that it had identified that it had breached SLC 23.6 in relation to four price increases in February and August 2008, and in February and August 2011 and breached SLC 24.3 in relation to two price increases in February and August 2011.
- 2.8. Limitations in E.ON's system in operation at the time required call centre staff to manually credit customer accounts using a "reason code", which would offset the impact of the price rise and any associated termination fees. E.ON's system could not avoid charging the price rise and associated termination fees in customers' final bills and required the manual input of the required code. Some agents failed to manually credit accounts, which resulted in the majority of customers that had notified E.ON of their intention to leave paying more than they should have (typically £10 - £20). Ofgem found that agents and team managers were not appropriately briefed to ensure processes were properly in place so that customers' accounts were correctly credited. Approximately 94,000 customers were potentially affected at the time.

⁵ SLC 23.6 set out that the notice period is triggered when a supplier is given notice (under the Master Registration Agreement for the purposes of the Electricity SLC's and under the Network Code for the purposes of the Gas SLC's) that another supplier will begin to supply the customer within a reasonable period.

- 2.9. E.ON implemented a redress scheme to customers and, in light of this action, a decision was taken by Ofgem not to take enforcement action and the informal investigation was closed in November 2012. Approximately £1.4m was paid out in compensation to 94,000 customers in January and February 2013. However, to reflect the seriousness of the breach, and the fact that E.ON may have gained as a result of consumers staying on with them to avoid the termination fee, in addition a goodwill payment of £300,000 was made to Age UK by E.ON in February 2013. A total of £1.7m in redress was paid and the results of the informal investigation were made public.
- 2.10. When closing the informal investigation in November 2012, Ofgem advised E.ON that, should information come to light that E.ON had contravened SLC 23 in respect of future price increases, in considering whether that contravention was a priority matter requiring investigation, Ofgem would:
- take into account any similarities with the 2008 and 2011 failures to comply with the requirements of SLC 23;
 - consider whether it should exercise any other enforcement power, including a provisional order in respect of such failures; and
 - invite the Authority, if at any time it was considering the level of financial penalty to impose in respect of any further breaches of SLC 23 by E.ON, to treat any similarities with the 2008 and 2011 failures as aggravating factors.
- 2.11. In its press release, dated November 2012, E.ON's Customer Service Director apologised and said "... Our systems are being updated to ensure this mistake can never happen again".
- 2.12. In response to the breaches it had committed and to prevent future breaches, E.ON told Ofgem on 18 July 2012 that it had established a new IT capability that required the ticking of a check box, to suppress charges, on those credit customers' accounts who notified their intention to leave. This new system (which E.ON referred to as "pinning" accounts to the old tariff) would ensure credit customers were not charged the higher prices.
- 2.13. In a letter, from E.ON's Director of Strategy and Regulation dated 30 January 2013 in response to a request from Ofgem, E.ON stated that it had its "enduring solution" in place in time for E.ON's price announcement date (10 December 2012) of its January 2013 price increase and that the solution had operated as intended.

3. The Authority's decision on contraventions

- 3.1. After considering all relevant information relating to the investigation, the Authority is satisfied that E.ON has breached SLCs 23.6 and 24.3. These breaches have been admitted by E.ON.
- 3.2. The Authority has made specific findings in relation to:
- SLC 23.6, in relation to E.ON's January 2013 price increase;

- SLC 24.3 in relation to E.ON's January 2013 price increase; and
- SLC 23.6 in relation to E.ON's January 2014 price increase.

Breach 1. *Breach of SLC 23.6 in relation to E.ON's January 2013 Price Increase:*

- 3.3. In relation to E.ON's January 2013 price increase, the Authority finds that E.ON failed to comply with SLC 23.6 by incorrectly charging customers higher prices from the date of the price increase (either 18 January 2013 or 7 March 2013 for credit customers) or the date the price was added to the meter (for PPM customers) until those customers left.
- 3.4. E.ON explained that the majority of its customers had been mailed in time for a price effective date of 18 January 2013 but that a 'mop-up' mailing had been required and therefore some customers had a price effective date of 7 March 2013. A small number of those customers had been affected. Throughout this document, the "mop-up" customers (a total of 135) are included among those affected by E.ON's January 2013 price increase.
- 3.5. The error relating to credit customers mainly occurred as customer services agents failed to tick a check box when customers gave notice to terminate their contract. Ticking the check box would have suppressed the price increase in the credit customer's final bill. The system for PPM customers was a manual process and ticking the check box should have allowed E.ON to identify those PPM customers who wished to switch so that they could then manually calculate and refund any monies due. By not ticking the box, these customers were not identified and refunds were not processed in a timely manner. Refunds were processed in April 2014, over a year after the January 2013 price increase contrary to SLC 23.6 which requires licensees to neither enforce nor take advantage of the price increase.
- 3.6. Based on the evidence supplied by E.ON, the Authority finds that between 6,150 and 23,655 customers who gave notice to terminate their contract, as a result of the price increase, were incorrectly charged those higher prices. The average higher charge calculated by E.ON was £8.60. The Authority notes that the actual number of customers affected by SLC 23.6 is unknown but is likely to be significantly less than 23,655 customers. E.ON tried to calculate the number of customers likely affected by doing sample checks. Based on those samples, it estimated that between 1,400 and 6,150 customers were likely to have been affected. The Authority has concerns regarding the methodology used and considers that the upper range provided by E.ON is likely to underestimate the likely number of customers affected.
- 3.7. The Authority acknowledges that E.ON paid redress of £201,219.95 to 23,414 customers potentially affected by this breach and that therefore those credit and PPM customers potentially affected will have been compensated. This payment included interest. The Authority acknowledges that, in relation to the remaining 241 customers that are deceased, E.ON proposes paying the monies owed, £2,106, to charity along with any uncashed cheques. The proposed charity is Citizens Advice Energy Best Deal Extra.

- 3.8. In respect of the further PPM customers (up to 510 customers) whom E.ON identified late in the investigation, the error occurred for a different reason. These were customers for whom the tick box was checked. The customers' details should have been added to a tasklist and passed to the appropriate operational team to manually calculate and refund any monies due. However, due to a lack of adequate oversight and monitoring control E.ON's system either did not add these customers details to the tasklist or the tasklist was not passed to the appropriate team to process any refunds due. Refunds for these customers have not yet been processed over two years after the January 2013 price increase contrary to SLC 23.6 which requires licensees to neither enforce nor take advantage of the price increase.
- 3.9. The Authority acknowledges that E.ON plans to make compensation payments to those further PPM customers that were affected by this breach by the end of April 2015 and intends to include a £10 goodwill payment, which would also cover interest. The total amount of compensation including goodwill payments is around £7,000.

Breach 2. *Breach of SLC 24.3 in relation to E.ON's January 2013 Price Increase:*

- 3.10. In relation to E.ON's January 2013 price increase, the Authority finds that E.ON failed to comply with SLC 24.3 by incorrectly charging termination fees.
- 3.11. Based on the evidence supplied by E.ON, the Authority finds that 882 customers, who notified E.ON of their intention to terminate their contract, were incorrectly charged termination fees. The fee charged was mainly £5 or £10.
- 3.12. The Authority acknowledges that 882 customers had been paid £8,337 in redress relating to the breach of SLC 24.3 in respect of the January 2013 breach. The termination fee refunded was mainly £5 or £10 and interest was added to this.

Breach 3. *Breach of 23.6 in relation to E.ON's January 2014 Price Increase:*

- 3.13. In relation to E.ON's January 2014 price increase, the Authority finds that E.ON failed to comply with SLC 23.6 by incorrectly charging credit customers higher prices from the date of the price increase, 18 January 2014, until the relevant customers left.
- 3.14. E.ON implemented a new automatic "Fixed Term Protection" system in response to Ofgem's Retail Market Review⁷ and informed Ofgem that it had been implemented and successfully tested in relation to its January 2014 price rise. The new system would automatically 'pin' credit customer accounts to the old tariffs and prevent higher charges from being applied upon notification of a new supplier taking on supply following a price increase. The Authority finds that the breaches occurred because of system errors, and that the system had not been fully tested before it was implemented.

⁷ The Retail Market Reform (RMR) was launched in late 2010 and has resulted in reform programmes to make the retail energy market simpler, clearer and fairer for consumers. By January 2014, complex tiered tariffs were banned, choosing a new deal was made easier and cash discounts were simplified.

- 3.15. Based on the evidence supplied by E.ON, the Authority finds that around 16,500 credit customers, who notified E.ON of their intention to terminate their contract, were incorrectly charged higher prices. E.ON was able to identify 15,192 of these customers through an automatic system update and the average price that was incorrectly charged to those 15,192 consumers was £12.12. A number of customers have yet to be identified and compensated and E.ON commits to making redress payments to the remaining customers affected.
- 3.16. The Authority acknowledges that a total of £184,127.04 has been paid in redress payments to these 15,192 credit customers identified. These redress payments excluded an interest payment. E.ON stated that, as monies were refunded within a few months, the amount of interest owed was nominal. E.ON calculated the total of amount of interest to be £7,365 and this figure has been included in the level of penalty.
- 3.17. In respect of the further PPM customers (around 6,500 customers) whom E.ON identified late in the investigation, the error occurred for similar reasons as set out in paragraph 3.8 for the January 2013 price increase, in that due to a lack of adequate oversight and monitoring control, the details of PPM customers who wished to switch were not added to the tasklist or the tasklist was not passed to the appropriate team to process any refunds due. Refunds for these customers have not yet been processed over one year after the January 2014 price increase contrary to SLC 23.6 which requires licensees to neither enforce nor take advantage of the price increase.
- 3.18. The Authority acknowledges that E.ON plans to make compensation payments to those further (around 6,500) PPM customers that were affected by this breach by April 2015 and intends to include a £10 goodwill payment, which would also cover interest. The total amount of compensation including goodwill payments is around £87,000.

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

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

- 4.1. The Authority has considered whether a financial penalty is appropriate in accordance with the requirements of the Electricity Act and the Gas Act and with its published Statement of Policy with respect to Financial Penalties (October 2003) ("the Policy"⁸). Under s27A(1) of the Electricity Act and s30A(1) of the Gas Act, the Authority may impose a penalty on E.ON of such an amount as is reasonable in all the circumstances of the case.
- 4.2. 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

⁸ <https://www.ofgem.gov.uk/ofgem-publications/74207/utilities-act-statement-policy-respect-financial-penalties.pdf>

further its principal objective⁹, having regard to its other duties. The Authority is not, under the Policy limited to considering the matters specifically mentioned in the Policy, but will consider all the circumstances of the case.

- 4.3. On 27 March 2014, the Authority published an open letter to its stakeholders setting out the Authority's position on future financial penalties (the "Chairman's Letter"¹⁰). In line with its strategic objectives for enforcement, the Authority stated that it considered that enforcement should deliver strong deterrence against non-compliance and also ensure regulatory compliance is given sufficient focus within businesses. As such, the Authority stated that it had decided to place greater emphasis on deterrence when imposing penalties and indicated that its decision would be likely to mean a substantial increase in the levels of penalty in cases where the behaviour in question came to the Authority's attention on or after 1 June 2014.
- 4.4. E.ON first notified Ofgem of its failure to meet its obligations under SLCs 23.6 and 24.3 in relation to the January 2013 price increase in November 2013. E.ON notified Ofgem of further potential breaches of these SLCs in relation to its January 2014 price increase on 13 June 2014 in respect of credit customers. On 15 February 2015, E.ON notified Ofgem of further potential breaches of SLC 23.6 in respect of PPM customers in relation to both the January 2013 and January 2014 price increases. As such, the position set out in the Chairman's Letter applies to the breaches of SLC 23.6 relating to the January 2014 price increase for both credit and PPM customers and to the breach of SLC 23.6 relating to the January 2013 price increase for PPM customers.
- 4.5. In deciding whether it would be appropriate to impose a penalty, the Authority has considered and taken into account the particular facts and circumstances of the contraventions under consideration, including the extent to which the circumstances from which the contraventions or failures arose may have been outside the control of E.ON. It has also taken full account of the representations made to it by E.ON.
- 4.6. The matters giving rise to considerations under the Policy are detailed 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

- 4.7. The Authority considers that the general interests of consumers and the market have been damaged by the contraventions set out in each of Breaches 1, 2 and 3. Breaches such as these have a wider impact on the energy market as consumer confidence in switching and trust in suppliers is vital for a healthy domestic

⁹ The Electricity Act (section 3A) and the Gas Act (section 4AA) set out the Authority's principal objective for energy regulation, thereby defining the purpose of Ofgem's activities as to protect the interests of existing and future consumers, wherever appropriate by promoting competition. The Energy Act 2010 amended the principal objective to clarify that the interests of consumers should be taken as a whole, including their interests in the reduction of greenhouse gas emissions and ensuring security of supply.

¹⁰ <https://www.ofgem.gov.uk/ofgem-publications/86815/theauthorityspositiononfuturefinancialpenaltiesletter27march2014.pdf>

energy market. PPM customers in particular are more likely to be vulnerable consumers as prepayment meters are used more often by households on low incomes. If consumers become disengaged and are put off from switching because of breaches of these rules then consumer inactivity could reduce the effectiveness of competition in the retail market. This is detrimental to the efficient functioning of the market.

- 4.8. The Authority also considers that the interests of E.ON's own consumers were damaged by the contraventions set out in each of Breaches 1, 2 and 3. Customers who wished to terminate their contracts with E.ON after receiving notification of price increases were incorrectly charged the higher rates until their contracts came to an end and/or were charged termination fees in contravention of licence conditions in place to protect consumers from these contraventions occurring.
- 4.9. The Authority acknowledges that compensation payments have been made to the majority of the customers directly affected by the breaches in this case (see below) and that those consumers should not have suffered any ongoing financial loss.

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

- 4.10. The Authority considers that imposing a financial penalty on E.ON is likely to incentivise compliance and help deter future breaches.
- 4.11. The Authority also considers that imposing a financial penalty is likely to send a message to the company, its shareholders and the industry at large that repeated breaches are taken seriously. It is incumbent on suppliers to take compliance with licence conditions seriously and they should take steps to do so proactively through putting appropriate systems and processes in place and checking that these systems and processes are effective. In the Authority's view, imposing a financial penalty will help to incentivise implementation of robust and stringent systems to prevent future breaches and ensure that any remaining improvement measures are put in place promptly.
- 4.12. Noting the position set out in the Chairman's Letter and, additionally, whilst the Authority acknowledges that E.ON took steps (and will take further steps) to secure compliance with SLC 23.6 and SLC 24.3, the Authority considers that the imposition of a financial penalty in relation to the January 2014 breach is warranted to reflect strong deterrence against future non-compliance by E.ON and other companies. The Authority also considers that imposing a financial penalty will create an incentive to ensure the underlying issues are fully and effectively addressed.

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

If the contravention is trivial in nature

- 4.13. The Authority considers that the contraventions were not trivial in nature and considers that the general interests of consumers and the market have been damaged by the contraventions (see paragraph 4.7). In relation to the January 2013 price increase, the Authority has found that between 6,150 and 23,655 credit and PPM customers were affected, with the average cost to each customer being £8.60 and that a further additional (up to 510) PPM customers were also affected. In relation to the January 2014 price increase, around 16,500 credit customers were affected, with the average cost to each customer being £12.12 and a further additional (approximately 6,500) PPM customers were also affected, with the average cost to each customer being £3.42.

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

- 4.14. The Authority does not consider that its principal objective and duties preclude 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

- 4.15. The Authority considers that the breach or possibility of a breach would have been apparent to a diligent licensee. E.ON was on notice of these issues following Ofgem's informal investigation in 2012 and fully aware of the need for extra vigilance to ensure compliance in this area.

5. Factors relevant to the level of financial penalty

- 5.1. In accordance with section 270(1) of the Electricity Act and section 300(1) of the Gas Act, the Authority may impose a financial penalty of up to 10 per cent of the annual turnover of the regulated person. The Authority is satisfied that its proposed penalty falls within the maximum statutory limit.
- 5.2. In deciding the appropriate level of financial penalty for the January 2013 and 2014 breaches, the Authority has considered all the circumstances of the case. It has also had regard to the following factors in accordance with the Policy.
- 5.3. In determining the level of financial penalty for the January 2014 breaches only, the Authority has also taken account of the position set out in the Chairman's Letter regarding deterrence as set out at paragraph 4.3 of this notice.

Factors which are first considered when determining the level of penalty

The seriousness of the contravention and failure

- 5.4. The Authority considers the contraventions described above are serious: consumer confidence is underpinned by suppliers complying with their legal obligations. The general interests of consumers and the market can be damaged by such contraventions since they impact on consumer confidence in switching

and trust in suppliers, which are vital for a healthy domestic energy market (see further at paragraph 4.7). In addition to the detriment suffered by directly affected customers in this particular case, the Authority considers compliance with SLCs 23.6 and 24.3 to be particularly important in protecting consumers, including potentially vulnerable PPM customers, wishing to terminate their contract after notification of a price increase.

- 5.5. The Authority also considers the fact that these are the fifth and sixth price increases giving rise to breaches of SLC 23.6 and the third price increase giving rise to breaches of SLC 24.3 to be of serious concern. The Authority acknowledges that all breaches were identified by E.ON and that the first four were investigated together as a single investigation.
- 5.6. Further, the Authority considers the fact that E.ON made representations which proved to be unreliable, to be serious. In its press release, dated 27 November 2012, E.ON's Customer Service Director stated that E.ON's systems were being updated to ensure this mistake could never happen again. In a letter to Ofgem dated 30 January 2013, the Director of Strategy and Regulation stated, in response to a request from Ofgem, that E.ON's "enduring solution" was in place in time for its price increase announcement date of 10 December 2012. This "enduring solution" was E.ON's new IT capability that required the ticking of a check box to suppress charges.
- 5.7. During the investigation E.ON provided details of the numbers of customers affected which proved to be incorrect. In a letter to Ofgem dated 23 May 2014, E.ON also gave the impression that its process for refunding PPM customers was robust. Whilst E.ON stated these statements were made in good faith, they proved to be unreliable and therefore have contributed to the seriousness of the contraventions.

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

- 5.8. The Authority considers that breaches such as those occurring in this case can cause serious harm to the general interests of consumers and the energy market. As noted in paragraph 4.7 above, such breaches can have a wider impact on the energy market as consumer confidence in switching and trust in suppliers is vital for a healthy and efficiently-functioning domestic energy market as a whole.
- 5.9. In determining the level of penalty, the Authority has taken into account that E.ON has made compensation payments to the majority of those customers affected or potentially affected by the breaches:
 - a) With regards to the January 2013 price increase, 23,414 customers were refunded in April 2014. The average compensation payment was £8.60 and the total repaid was £201,219.95. The remaining 241 customers are deceased. E.ON proposes paying the monies owed, £2,106, to charity along with any uncashed cheques. The proposed charity is Citizens Advice Energy Best Deal Extra.

- b) In relation to the January 2014 price increase, 15,192 customers (out of the around 16,500 customers affected) were refunded incorrect higher prices in September 2014 although interest was not paid. The average compensation payment was £12.12 and the total repaid was £184,127.04. E.ON has calculated the interest owed to be £7,365 and the Authority has included this in the level of penalty.
- c) In relation to the further PPM customers affected (up to 510 customers for the January 2013 price increase and around 6,500 customers for the January 2014 price increase), the Authority acknowledges that E.ON plans to make compensation payments and intends to include a £10 goodwill payment, which would also cover interest. The total amount of compensation including goodwill payments to be paid to these customers is around £94,000.

The duration of the contravention or failure

- 5.10. The breaches of SLCs 23.6 and 24.3 occurred at particular points in time in respect of E.ON's January 2013 and January 2014 price increases. However, the Authority considers the repeated nature of the contraventions, over consecutive price increases, to be a serious matter demonstrating continued non-compliance with the applicable SLCs.
- 5.11. The Authority acknowledges that E.ON has proposed to undertake an independent external audit to provide assurance regarding compliance. E.ON has also confirmed it will implement any appropriate recommendations made by auditors relating to non-compliance of SLCs 23.6 and 24.3 prior to any future price increase. However, noting the position set out in the Chairman's Letter, the Authority considers that the level of any penalty relating to the January 2014 breach must reflect the importance it places on deterring future breaches.

The gain (financial or otherwise) made by the licensee

- 5.12. While E.ON did invest in a new system after the breaches that occurred in relation to the price increases informally investigated in 2012 and again after the January 2013 breaches were uncovered, the Authority considers that E.ON could have gained financial benefit as it had not properly trained staff to use the check box system in relation to the January 2013 breaches. In addition, given the seriousness of the issue, and previous occurrences of the same breaches, the Authority considers that E.ON should have put in place adequate compliance and monitoring checking procedures and, by not doing so, has gained financially through avoided costs. In relation to the manual process for PPM customers, the Authority considers that there was inadequate management oversight and monitoring procedures in place to ensure E.ON's system generated the tasklist and that it did so accurately, and to ensure that this was passed to the appropriate operational team for refunds to be paid in a timely manner.
- 5.13. The Authority further considers that E.ON has also gained financially through avoided costs because it did not carry out robust testing of its new Fixed Term Protection system, which led to the breaches in relation to the January 2014 price increase.

- 5.14. It is the Authority's view that had E.ON taken its compliance obligations more seriously then it would have spent a considerable amount more on putting in place proper and robust systems, processes and monitoring and compliance procedures to check that their systems were effective in ensuring compliance with the licence conditions.
- 5.15. The Authority notes that the majority of consumers have been compensated for their direct financial losses as a result of these breaches and that E.ON intends to compensate the remainder by the end of April 2015. However, taking all of the circumstances of the investigation into consideration, the Authority considers that E.ON has gained financially as a result of avoided compliance costs.

The Authority's position concerning deterrence of future breaches (Breach 3 only)

- 5.16. In setting the level of penalty for the January 2014 breaches, the Authority has also taken into consideration its stated position on deterrence of future breaches as set out in the Chairman's Letter.
- 5.17. As set out at paragraph 4.3, the Authority considers that enforcement should deliver strong deterrence against non-compliance and ensure regulatory compliance is given sufficient focus within businesses. The Authority's decision to place greater emphasis on deterrence in its enforcement work will be reflected in the level of financial penalties it imposes in appropriate cases.
- 5.18. The Authority has carefully considered the circumstances of the January 2014 breach, including E.ON's actions with regard to regulatory compliance. It has taken into consideration the repeated nature of the breaches, that potentially vulnerable consumers have been affected and the fact that the underlying problems with E.ON's internal systems and processes still remain to be fully and effectively identified and resolved. In view of this, the Authority considers that the penalty it imposes in respect of Breach 3 must act to deter future breaches and reinforce the need for senior management to ensure regulatory compliance going forward. These considerations are reflected in the higher penalty imposed on E.ON in respect of Breach 3.

Factors tending to increase the level of penalty

Repeated contravention or failure

- 5.19. As stated above, E.ON self-reported a breach in 2012 of SLC 23.6 in relation to four price increases in February and August 2008, and February and September 2011 and SLC 24.3 in relation to two price increases in February and September 2011. Given these previous breaches, E.ON would have been aware of the requirements of the relevant SLCs and the seriousness with which the Authority would view any future breaches.

- 5.20. The Authority considers it a significant aggravating factor, that despite the previous breaches, E.ON did not take the necessary steps to ensure compliance and the breaches recurred in respect of the January 2013 and January 2014 price increases. The Authority considers that E.ON should have taken steps to ensure all its processes and procedures, including for PPM customers, were compliant with SLCs 23.6 and 24.3 and that it should have been on alert from the previous breaches to check all areas of its business to ensure compliance. The Authority considers that these breaches would have been avoided if E.ON had placed sufficient emphasis on ensuring compliance and checking all its relevant processes and procedures. Whilst steps were taken after the previous contravention, for both the January 2013 and January 2014 price increases, the systems, procedures, training of staff, monitoring and compliance that were put in place, fell short of ensuring compliance.
- 5.21. For these reasons, the Authority considers this to be a significant aggravating factor.

Continuation of contravention or failure after either becoming aware of the contravention or failure or becoming aware of the start of Ofgem's investigation

- 5.22. The contraventions in this case have occurred following price increase notifications and the Authority notes that E.ON has agreed to undertake an independent external audit and to implement any appropriate recommendations made by auditors relating to non-compliance of SLCs 23.6 and 24.3 prior to any general price increase.
- 5.23. However, the Authority is concerned that these contraventions continued after E.ON became first aware of them through Ofgem's informal investigation in 2012. The Authority recognises that these contraventions were not deliberate or calculated, but considers that this aggravating factor applies.

The involvement of senior management in any contravention or failure

- 5.24. The Authority considers that having experienced a previous breach of the SLCs, senior management should have been expected to ensure that adequate steps were put in place to avoid the risk of similar breaches occurring again in relation to any future price increases. This includes for all processes and procedures that could have been affected, including for PPM customers.
- 5.25. In relation to the January 2013 price increase, E.ON implemented a new system following the 2012 breaches and statements were given at a senior level that this was robust. However, this did not prevent the breaches of the SLCs recurring.
- 5.26. In relation to the January 2014 price increase, E.ON implemented a new automatic "Fixed Term Protection" system and informed Ofgem that it had been implemented and successfully tested in relation to its January 2014 price rise. The Authority found that the new system had not been fully tested before it was implemented and that system errors led to a further breach of SLC 23.6.

- 5.27. While we consider that E.ON's senior management were not actively involved in any deliberate actions in relation to these contraventions, senior management were well aware of the problems relating to E.ON's system over a significant length of time following Ofgem's investigation in 2012 and failed to take sufficient steps to prevent the breaches from reoccurring. For this reason, the Authority considers this is to be a significant aggravating factor.

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

- 5.28. The Authority notes that E.ON put certain systems and procedures in place to prevent contraventions or failures. In respect of the January 2013 price increase, it put new procedures in place and carried out training of staff. In respect of the January 2014 price increase, it carried out testing of its new IT system designed to prevent the previous breach. However, the Authority notes that the systems, testing, training and procedures put in place were inadequate to prevent the breaches and that a lack of management oversight and monitoring control resulted in the breaches relating to PPM customers not being identified and reported until late in the investigation.
- 5.29. Taking the above into account, the Authority does not consider there was an absence of any evidence of internal mechanisms or procedures *intended* to prevent contravention or failure. Accordingly, the Authority considers that this aggravating factor does not apply.

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

- 5.30. E.ON did not conceal the contraventions from Ofgem, and the Authority acknowledges that E.ON self-reported the contraventions in relation to the January 2013 price increase and, to a lesser extent, the contravention in relation to the January 2014 price increase (see paragraphs 5.42 to 5.45). The Authority also acknowledges that E.ON self-reported the breaches relating to PPM customers albeit late in the investigation. The Authority considers that this aggravating factor does not apply.

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

- 5.31. The Authority acknowledges that E.ON did take certain steps towards achieving compliance, but it is of the view that there were significant inadequacies in its approach. The Authority considers that this mitigating factor applies to a limited extent for the reasons set out below:

Securing compliance in relation to the January 2013 price increase:

- 5.32. Whilst E.ON explained that it had carried out training, by way of briefings in the form of daily updates and communications in routine team meetings to all staff,

and further briefings to managers reminding them of the new processes, the Authority considers the steps taken did not prevent the problem recurring and E.ON did not adequately put in place training that secured compliance.

- 5.33. E.ON provided evidence of a Managers Survey that it had carried out to verify that training had been delivered to staff. The Authority finds that the survey was not carried out in time, was only completed by a small number of managers with no follow-up action carried out and was therefore inadequate in securing compliance.
- 5.34. The Authority finds that there was insufficient evidence to show that thorough and effective compliance monitoring took place, and finds there was inadequate communication in relation to the importance of compliance monitoring.
- 5.35. The Authority finds that in relation to the manual process for PPM customers, E.ON did not have adequate management arrangements and monitoring procedures in place to ensure compliance with SLC 23.6.

Securing compliance in relation to the January 2014 price increase:

- 5.36. The Authority finds that, whilst E.ON took steps to test its new “Fixed Term Protection” system, in preparation for the price increase, these were inadequate and resulted in significant failings relating to price protection in respect of the January 2014 price increase. E.ON submitted that, for the majority of customers affected by the price increase, where price protection had failed, not all scenarios had been tested.
- 5.37. As set out above, the Authority finds that in relation to the manual process for PPM customers, E.ON did not have adequate management arrangements and monitoring procedures in place to ensure compliance with SLC 23.6.

Appropriate action by the licensee to remedy the contravention or failure

- 5.38. The Authority finds that the steps E.ON put in place to remedy the contravention in relation to the January 2013 price increase, implementation of its new “Fixed Term Protection” system, were inadequate due to insufficient testing.
- 5.39. The Authority notes that E.ON proposes to carry out an independent external audit to remedy the contravention in relation to the January 2014 price increase. The Authority acknowledges this action to be a positive step towards securing compliance. The audit is due to be carried out in April 2015 and will look at IT project governance, IT systems, effectiveness of delivery, compliance processes, training and communications and redress for customers when assessing E.ON’s compliance with SLCs 23.6 and 24.3. E.ON has agreed to implement any appropriate recommendations made by auditors relating to non-compliance with SLCs 23.6 and 24.3 prior to any general price increase.
- 5.40. Having taken account of the points set out above, the Authority considers this mitigating factor applies to a limited extent.

Evidence that the contravention or failure was genuinely accidental or inadvertent

5.41. The Authority recognises that the contraventions were not deliberate or calculated. Having said this, these are the fifth and six instances of breach of SLC 23.6 and the third instance of breach of SLC 24.3 in relation to E.ON's price increases and the Authority considers that, at a certain point, such repeated behaviour must be treated as amounting to disregard of the licence obligations. The breaches in relation to the January 2013 and January 2014 price increases occurred after the breaches in 2012 and E.ON were fully aware from these earlier failures of the requirements of the SLCs. Although the Authority recognises that management tried to rectify the breaches after the January 2012 investigation, the systems that were put in place were not robust, tested thoroughly or adequate to secure compliance. In view of the above, the Authority considers that these contraventions cannot be regarded as genuinely accidental or inadvertent and therefore this mitigating factor does not apply in this case.

Reporting the contravention or failure to Ofgem

5.42. E.ON self-reported contraventions of the SLCs in relation to the January 2013 price increase on 22 November 2013 but the Authority has concerns regarding the promptness of that self-reporting. The Authority found that Senior Management were aware of the potential repeat breaches four months before reporting them. Furthermore, the Authority found that a post-implementation review could have been carried out three months earlier and therefore the issues flagged and reported to Ofgem earlier. The Authority acknowledges that E.ON waited before reporting these breaches as it wanted to provide a comprehensive report. The Authority acknowledges that the adequacy of the self-reporting relating to Breaches 1 and 2 was not an issue but considers that promptness was an issue.

5.43. E.ON notified Ofgem on 13 June 2014 of further potential breaches of the SLCs in relation to its January 2014 price increase. The Authority acknowledges that E.ON provided the information available to it at that time, but considers that the notification was not sufficiently clear or detailed enough to amount to self-reporting to a regulator. The Authority found that Breach 3 was reported on the same day that an information request was sent to E.ON asking for evidence that the new system that it put in place to prevent future breaches (its "Fixed Term Protection" system) had secured compliance in relation to its January 2014 price increase. The Authority considered that the failure would have come to light through the investigation in any case.

5.44. In relation to the breach of SLC 23.6 in respect of PPM customers for both the January 2013 and January 2014 price increases, although E.ON notified Ofgem late in the investigation, the Authority noted that E.ON had done so as soon as it became aware of the issue.

5.45. The Authority therefore considers that this mitigating factor applies to some extent in respect of Breaches 1 and 2, but only to a limited extent in respect of Breach 3.

Co-operation with Ofgem's investigation

5.46. The Authority expects companies to cooperate fully with Ofgem's investigations and considers that this mitigating factor should apply only where such cooperation has gone well beyond what would be expected of any regulated person facing enforcement action. E.ON accepted the breaches and agreed to settle the case at the earliest opportunity and this has achieved a speedier resolution and avoided additional spending of resource by the regulator. For that reason, the Authority considers that E.ON has fully co-operated with Ofgem's investigation and accordingly, considers this mitigating factor applies.

6. The Authority's decision

- 6.1. The Authority has considered all of the circumstances of the investigation. It considers that the seriousness of the contraventions, the repeated nature of the breaches and the level of involvement of senior management in failing to take sufficient steps to prevent the breaches from reoccurring warrant a financial penalty.
- 6.2. The penalty proposed for Breaches 1 and 2 is substantially lower than that proposed for Breach 3. In part, this is because E.ON has the benefit of reporting Breaches 1 and 2 (with the exception of the further PPM customers identified late in the investigation) before consideration of the Chairman's Letter became applicable in June 2014.
- 6.3. The Authority considers that Breach 3 requires a penalty which takes into account the further repetition of the breach of SLC 23.6, including in relation to potentially vulnerable PPM customers, and, in addition, reflects the Authority's position set out in the Chairman's Letter relating to deterrence. In accordance with this, the Authority considers that the proposed level of penalty to the extent it relates to Breach 3 is required to deter future breaches and help ensure that regulatory compliance is given sufficient focus within the business in the future.
- 6.4. Taking all the above into account, the Authority considers it appropriate in the circumstances of this investigation to impose a penalty of £1 on E.ON provided that, as at the date of any Final Penalty Notice, and at a date to be notified by the Authority, E.ON has paid £7,750,000 (less £1) by way of consumer redress as set out at paragraphs 1.7 and 1.8 above. The Authority considers the proposed penalty to be reasonable in all the circumstances of the case. In reaching this decision the Authority has considered in particular the following:
- (a) These are the fifth and six instances by E.ON of breaches of SLC 23.6 and the third instance of SLC 24.3 around price increases and the repeated nature of these breaches is a serious concern;
 - (b) Around 6,500 potentially vulnerable PPM customers have been affected by the breach of SLC 23.6 in respect of the January 2014 price increase;
 - (c) Senior management at E.ON were aware of the previous investigation in 2012 and failed to take sufficient steps to prevent the breaches recurring;

- (d) The position set out in the Chairman's Letter in relation to the breach of SLC 23.6 in respect of the January 2014 price increase including in respect of PPM customers;
- (e) Between 29,660 and 47,165 customers were affected in total and E.ON has paid redress totalling £395,789.99;
- (f) Three aggravating factors apply (see paragraphs 5.19-5.27);
- (g) Certain mitigating factors apply (see paragraphs 5.31-5.40 and 5.42-5.46);
- (h) E.ON has admitted the breaches in this case; and
- (i) E.ON has agreed to settle the investigation, including making a payment of £7,750,000 (less £1) in consumer redress.

- 6.5. Any written representations or objections with respect to the proposed penalty must be received by Andrea Gregory (andrea.gregory@ofgem.gov.uk) at Ofgem, 9 Millbank, London, SW1P 3GE by 5pm on 5 May 2015.
- 6.6. Any representations or objections received may be published on the Ofgem website. Should you wish your response or part of your response to be confidential, please indicate this clearly and give reasons for this request. Any such requests will be considered by Ofgem on a case by case basis.

Gas and Electricity Markets Authority

2 April 2015