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**24 August 2016**

Dear Kieran,

**Response to consultation 'Allocation of voluntary redress payments in the context of enforcement cases'**

This submission was prepared by Citizens Advice. Citizens Advice has statutory responsibilities to represent the interests of energy consumers in Great Britain. This document is entirely non-confidential and may be published on your website. If you would like to discuss any matter raised in more detail please do not hesitate to get in contact.

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**Question 1: Do you agree with our objectives for the allocation of voluntary redress? If not, please explain why.**

Yes.

**Question 2: Are there any additional objectives or criteria we should consider when making a decision on our forward approach to voluntary redress? Are there things our approach should definitely include or absolutely avoid?**

We agree with the approach as set out. In particular it is important that the process ensures high quality bids for funds are selected, and that robust monitoring and reporting is in place to ensure that these maximise benefit to consumers.

**Question 3: What are your views on 'Option 1: Current process with enhanced principles'? Are there any other advantages, disadvantages, risks or costs relating to this option that we should consider?**

We do not consider that this option is the best way to deliver the aims and objectives set out in chapter 2. We are concerned that this option carries the significant risk of extending the timeline for the settlement process, which could delay consumers directly affected by the company's actions from receiving direct redress and increase the costs of enforcement.

The option requires both the regulator and energy companies to act outside of their core competencies. It places greater administrative burdens on Ofgem, and also requires energy companies under investigation to set up and run competitive processes when they agree to make redress payments.

It also has additional burdens for charities and organisations applying for funds, as there will continue to be variations in the funding allocation process, on a case by case basis. This may act as a barrier to a wide range of groups being able to apply for funding. The option precludes more innovative approaches, for example moving to a periodic funding process, which could also make the application process easier for a range of charities.

**Question 4: What are your views on the possible additional principles outlined in 'Option 1: Current process with enhanced principles'? Are there further additional principles that would help meet our objectives?**

We have set out our views on each of the additional principles below. The consultation document does not make clear whether Ofgem is proposing that these principles would also apply to Option 2 (the allocation of funds by an expert third party). Where we are supportive of additional principles we consider that these should apply to both options.

*The number of charitable recipients should be proportionate to the size of the penalty*

We disagree with the proposal that the number of recipients should be proportionate to the size of the penalty, as this seems an arbitrary and risks conflicting with the main objective that funding maximises consumer benefit. The process of allocating funds should be designed in such a way to remove barriers for smaller charities bidding, but should not compromise on the principle that funding is awarded based on the quality and suitability of the bids, and the ability of the organisation to deliver it. Similarly, neither should the process preclude charities on the basis that they have previously been awarded redress payments. The overriding principle should be that redress funding is awarded to charities that deliver quality projects to vulnerable consumers and that they are able to demonstrate that this achieves real outcomes using appropriate reporting and monitoring.

We set out some further ideas around how to enable increased diversity in fundees in response to question 8.

*The allocation of voluntary redress payments to charities or trusts that were established by the company under investigation and/or whose name contains a reference to that company should be precluded*

We agree that charities with the name of the company under investigation should be precluded. Furthermore, we recommend that all charities with a name that refers to an energy company, or those that were established by an energy company, should be precluded from all bidding for redress payments. Companies under investigation may be unwilling to make redress payments if these could ultimately provide good publicity for their competitors. Similarly, a situation could arise in which a company making a redress payment in relation to one investigation simultaneously has a related charitable arm allocated funds from the redress payments related to an investigation into another company. This would lead to a similar end result to that which Ofgem are seeking to avoid, in which companies with poor practices benefit from the allocation of redress payments.

*An open bidding process should be used to select recipients*

We agree that an open, competitive bidding process should be used. This should assess bids on a number of areas, including: the level of benefit to be delivered to energy consumers, the organisation's experience in dealing with consumers' energy issues, the organisation's capacity to commence delivery in the agreed timeframe, the targeting of the proposal at the harm caused, and the ability and experience of the organisation in engaging with vulnerable consumers (including any vulnerabilities specific to the harm caused). Ofgem (or a third party, if appointed) should consult on the criteria at a later point.

The bidding process should also be designed to allow existing projects to bid for funding to either continue or expand their work. Such projects may be more cost effective, as they will require less funding to spend on development and able to devote more to delivery for the benefit of consumers.

The bidding process should be conducted in line with the relevant section of the Fundraising Regulator's Code of Fundraising Practice<sup>1</sup>, and should include a limited appeals process for cases where bidders feel that there were mistakes of fact, or where decisions were not reached in accordance with the published rules and guidance on fund allocation.

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<sup>1</sup> <https://www.fundraisingregulator.org.uk/wp-content/uploads/2016/06/Code-of-Fundraising-Practice-v1-3.pdf> (see Section 10 - Trusts)

*Money should be used to support vulnerable energy consumers (with a specific focus on supporting their energy-related needs)*

We agree that money should be focused on vulnerable consumers and their energy-related needs. This should be based on an understanding of vulnerability as related to both personal circumstances and the structure of the energy market and energy products. Vulnerability can also be transitory as personal circumstances change. Redress funding should seek to address the harms of the actions of energy companies where these affect individual vulnerable groups, but where this is not the case we would expect that funding should be allocated in such a way that ensures that a range of vulnerable circumstances are addressed.

*Recipient organisations, including indirect recipients, should be told that the money they receive is a result of enforcement action*

We agree that all recipient organisations, including indirect recipients, should be told about the origin of the money they receive. This requirement should not extend to consumers benefiting from projects, as this would add further administrative burden, and could have the impact of undermining the consumer's trust in the energy market.

*Potential recipients must demonstrate they can and will monitor and regularly report on the impact of the funding they receive*

We agree that recipients must be able to demonstrate they can monitor and report on the impact of funding. In line with better regulation principles, these requirements should be proportional to the size of the funding award. This will minimise risk, by focusing oversight on larger awards, while not placing overly burdensome requirements on smaller organisations receiving smaller sums of money.

In setting the monitoring and reporting framework, Ofgem (or a third party) should seek to limit this to such a level required to ensure delivery quality and minimal risk. This should enable a larger proportion of the redress funding to be used to deliver benefit to consumers, and less on monitoring and reporting. It should also improve the experience of the consumers that benefit from these projects, by limiting the amount of demographic and feedback materials they are required to fill in.

Where the initial recipient plans to disburse funds to secondary groups, the initial recipient should retain responsibility for the actions of indirect recipients, and

demonstrate that they are capable of monitoring the use of these funds by secondary groups.

**Question 5: What are your views on 'Option 2: Responsibility given to a third party with appropriate expertise'? Are there any other advantages, disadvantages, risks or costs relating to this option that we should consider?**

We consider that this option has a number of advantages. This option will reduce the burden on Ofgem and companies, and ensure that allocation decisions are taken by experts in the charitable sector. This should ensure that redress payments are provided to projects that maximise the benefit of the funds for the benefit of consumers. It could also enable more innovative ways of allocating money, through phased funding and periodic allocations, and reduce the barriers to smaller charities applying for funding.

In order to retain clear responsibility and accountability under this option, Ofgem should retain responsibility for the final decision on allocations. However, we would expect that if the expert third party is performing in line with its guidance there should be very few circumstances in which the regulator will disagree with the recommendation of the third party. In order for charities to retain confidence in the process of allocation, Ofgem should set out the circumstances in which they would disagree with a recommendation. Such circumstances could include cases in which Ofgem is privy to industry information which suggests that the allocation is inappropriate. Where decisions to block funding are made, these should be publicly available.

The consultation raises the opportunity that using a third party could allow for payments to be allocated on a periodic, rather than a case-by-case basis. We agree that periodic allocation could have a number of benefits. Smaller redress payments may become more common in future as the number of suppliers in the market increases, and periodic allocation could pool these payments to realise economies of scale for the allocation and use of these funds. It would also provide a stable process for charitable organisations by providing funding regularly, rather than on an ad hoc basis (albeit with varying amounts of funds each period). Within these periodic allocations it should still be possible to create guidance for the third party and bidders to ensure that proposals target the nature of the breaches across the period. Periodic allocation could also better ensure funding achieves an appropriate geographic spread, and reaches a full range of vulnerable consumers. This approach could cause a delay in consumers receiving the benefit of the redress

payments, and the third party should mitigate this by ensuring that the allocation process is completed in a timely manner.

If a periodic approach is taken, energy companies should be required to hand over the funds at the point at which the case is settled, rather than the point in the period in which the allocation is made and agreed. This will allow funds to be managed by the third party to earn interest or investment income until they are allocated.

We also support the potential introduction of phased or multi-year payments where appropriate. This could give more certainty to charities and allow longer term projects to be supported, while making future installments of funds dependent on ongoing quality of delivery would ensure projects are delivered to a high standard and protect the redress funds from being used ineffectively. We would not support energy companies retaining these funds if phased allocation is introduced. Ofgem's Statement of Policy with respect to Financial Penalties and Consumer Redress' already has regard for the financial viability of the company when settling cases. Once the redress levels are set, we consider that a better alternative would be for the third party to hold the funds for investment or to earn interest.

In order to maximise the funding going to consumers, it is important that Ofgem procures a third party with relevant expertise at the lowest cost. This will particularly be the case if it is decided that the costs of the third party should be paid either from redress funding or interest/investment income, rather than our preferred approach that these costs are paid by companies (although even in the latter case, low administration costs would encourage companies to continue making voluntary redress payments). If the procurement process results in proposed costs that are substantially higher than Ofgem's expected range of 0.5-1.5% the regulator may want to reconsider whether this option is the most appropriate. Ofgem may want to mitigate this risk by carrying out more market testing with potential providers before beginning the procurement process.

The contract for the third party should ensure that there are strict quality controls for delivery of the bidding and allocation process. Ofgem should ensure that the successful bidder has the capacity to consider the full range of energy issues that redress payments may relate to, and are able to work with a range of types of organisations which may apply for funds. The regulator may also want to consider whether there may be conflicts of interest for some third parties if they also administer energy company charitable funds. Ofgem should take steps to minimise these risks, or get assurances on how they would be managed by the third party.

The third party should carefully monitor and report to Ofgem on the use of money by the recipients of funds. These reports should also be publicly available to track the use and impact of redress payments, and to share best practice. In addition, Ofgem should monitor and report on the performance of the third party - including feedback from both successful and unsuccessful bidders and the financial performance of any funds under management - in order to ensure they are meeting the standards set out in their contract and to inform future procurement decisions. Feedback from bidders and from the third party should also be used to improve Ofgem's guidance on allocating funds over time.

**Question 6: How should the costs of the third party associated with allocating redress be funded?**

We consider that companies paying redress to consumers should cover these costs in line with the current process, in which companies face administration costs when allocating redress payments. This could be recouped either as a fixed percentage of the total redress paid by the company, or a fixed fee per payment of redress, or a combination of the two. Ofgem should ensure that companies do not simply attempt to reduce the level of redress payments in order to cover these administration costs.

We do not agree that the third party costs should be taken from the redress funding. All of the redress funding provided by companies should be made available for allocation to organisations delivering projects for the benefit of consumers.

We are not supportive of interest or investment earnings from the redress fund being used to cover these costs. These earnings will arise only when redress has been retained and not yet used for its intended purpose and should be used to protect the real value of the redress funds.

**Question 7: Should the company that made the redress payment have an input into the approval of recipients under this option?**

The third party should retain independent control of the bidding process. However, we recognise that companies may be more willing to make voluntary redress payments if they are able to provide an input into the allocation of funds, and that this may ensure they consider the impacts of their behaviour. Points at which they could have an input would therefore be when Ofgem is preparing guidance on fund allocation for the third party, and/or when Ofgem makes a final decision on the recommendation made by the third party. At the point when guidance is developed the company could usefully feed in demographic data on the types of consumers

affected by their behaviour and other insights in relation to how they had been affected. Any input from the company at the final decision stage should be limited to cases where they are able to show that the decision by the third party was not in line with the allocation guidance or processes. Ofgem would need to consider how they take account of different company inputs if allocations were made on a periodic basis, as payments could be derived from a combination of redress from different companies.

**Question 8: How can we ensure that smaller potential recipients can bid and are not disadvantaged compared to larger potential recipients?**

The delivery of the bidding and allocation process by a third party should reduce the barriers that smaller charities have previously faced in gaining for redress payments, by having a single allocation process and by being able to provide clear guidance and advice to potential bidders. A periodic allocation approach would also give certainty over the timelines of each allocation. Ofgem will also be able to enable participation by providing guidance on funding requirements in a clear and timely manner, in order that charities have to time to prepare well targeted bids.

However, the third party may also consider the economies of scale associated with larger charities, and that a very large number of smaller charities being awarded funds would increase the monitoring and reporting requirements for the third party. The third party should have the flexibility to award funding to national charities with the capacity and infrastructure to engage with, and disburse funds to, a large number of smaller geographically spread charities. Such national charities may be able to offer a consistent service delivery and outcomes framework, reducing local set-up time and set-up costs which would deliver benefits to consumers faster, and reduce the administrative costs of the third party.

A proportionate system of monitoring and reporting requirements should ensure that there is a match between the size of awards for charities and their capability to meet the requirements. This could even extend to the third party reserving a small proportion of the total redress funds to be made available as micro grants to charities, with minimal reporting and monitoring requirements. Over time this could help enable capacity building for charities to apply for more funding in subsequent allocation rounds.

Taken together these measures could achieve a level playing field for all bidders. However, the overriding principle of the bidding process should continue to be that it allocates funds to the highest quality bids, which best meet the allocation criteria.



**Question 9: What are your views on this 'Variation on Option 2 – Voluntary redress payments go to a charitable trust set up by Ofgem'? Are there any other advantages, disadvantages, risks or costs relating to this option that we should consider, particularly in relation to the DAF provider model set out above?**

We do not support this option. It would incur a large amount of investment of resource from the regulator to set up, as well as ongoing running costs. Given that redress payments are variable from year-to-year, the infrastructure of the trust could at times be redundant or underused. Our preference would be a third party option, whereby the costs incurred are proportional to the redress payments that are made. It may only be viable to develop a trust if this retained some funds to pay out in later years, which would delay the point at which these could be used to support consumers.

**Question 10: How should the costs of running a charitable trust set up by Ofgem be funded?**

The ongoing costs under this option should be paid by companies making redress payments, in line with the current process. However, it may be difficult to determine how to recover these costs from companies. Assuming that a larger proportion of the costs are fixed under this option (as compared to the use of a third party), then if there are relatively low redress payments in a particular year then this could require disproportionately high administration fees from companies, or for the shortfall to be met from redress payments or by Ofgem. In contrast, under the option of a third party with charges proportional to the level of redress payments it would be easier to recover these costs from companies paying redress.

**Question 11: What are your views of the idea of using part of voluntary redress payments to support specific schemes? What are the advantages, disadvantages, risks or costs relating to this idea? What existing schemes could be considered under this approach?**

We do not support the use of voluntary redress payments for energy schemes run by non-charitable organisations. We are concerned that unless any funding from redress payments for such programmes coincided with an increase in their scope this would likely lead to a decrease in other funding streams, and therefore not deliver additional benefit to energy consumers. Supporting particular schemes on an enduring basis would also undermine the principle of an open and competitive bidding process to select the best projects. It could also undermine the principle that redress funding should be targeted at the particular harm caused by a

company's actions. Given the aims of Big Energy Saving Network we consider that this programme should continue to be funded by Government.

Finally, as pointed out in the consultation, the value of support would vary year-on-year and would not therefore be suitable for providing stability to ongoing programmes delivered by non-charitable organisations.

**Question 12: Which of the options in this consultation do you think should be used and why?**

We consider that Option 2 (the use of a third party to allocate voluntary redress payments) best meets Ofgem's objectives, as well as the enhanced principles we have indicated our support for. This process should ensure that allocation decisions are made by an organisation with expertise in this area, and ensure transparency of how and why decisions are made.

**Question 13: Should any other options be considered? If so, please provide an outline explanation of your suggested alternative option(s). Please also outline any associated benefits and costs with the alternative option(s).**

If Option 1 is taken forward, a potential enhancement could be for Ofgem to develop and hold a pre-selected list of projects which meet certain funding criteria. This list could be developed using a competitive process. This would reduce the risk that Option 1 could add significant delays to the case settlement process, and also remove the requirement for companies to develop and run competitive processes for redress allocation. This option may be more suitable for continuing funding for established projects with a good track record of delivery. Charities develop considerable expertise when setting up and delivering projects which would be lost if funding stopped.

If you have any questions about this consultation response, or would like to discuss any of the issues raised, please do not hesitate to contact me.

Yours sincerely,

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