

Notice of Decision to impose a financial penalty pursuant to section 30A(5) of the Gas Act 1986 and / or section 27A(5) of the Electricity Act 1989

Decision of the Gas and Electricity Markets Authority to impose a financial penalty, following an investigation into compliance by British Gas with the requirements of Article 9(1) and Article 9(1A) of the Electricity and Gas (Carbon Emissions Reduction) Order 2008 (as amended)

5 March 2015

1 Summary

1.1 The Gas and Electricity Markets Authority (“the Authority”) has decided to impose a financial penalty of £1 on British Gas¹, on the basis that British Gas has made a payment of £500,000 (less the £1 financial penalty) in consumer redress to the British Gas Energy Trust (“BGET”). The BGET shall distribute the redress monies to organisations which pursue any or all of the following objectives² for vulnerable customers:

- the promotion of energy efficiency in domestic homes;
- the alleviation of fuel poverty;
- the reduction of carbon emissions in domestic homes

1.2 This follows an investigation by Ofgem into British Gas’ failure to meet its obligations under the Electricity and Gas (Carbon Emissions Reduction) Order 2008 as amended³ (“CERT Order”), and consideration by the Authority of representations or objections received on its proposed penalty. These representations or objections are discussed in the Annex to this Penalty Notice.

1.3 Under Article 9(1) and Article 9(1A) of the CERT Order, gas and electricity suppliers had to achieve their carbon emissions reduction obligations by promoting qualifying actions to domestic energy users in Great Britain. British Gas was required to achieve carbon savings to meet an overall CERT target and also to meet sub-obligations which included an Insulation Obligation (IO) target.

¹ The CERT Order placed obligations on individual British Gas licensees. References in this Penalty Notice to British Gas shall include reference to those licensees: British Gas Trading Limited (Electricity) and British Gas Trading Limited (Gas).

² The Authority requires that any consumer redress must not adversely interfere with the delivery of other energy efficiency schemes such as the Energy Companies Obligation (ECO), or create an unreasonable administrative burden for Ofgem.

³ The CERT Order was amended by the Electricity and Gas (Carbon Emissions Reduction) (Amendment) Orders of 2009 & 2010, the Electricity and Gas (Community Energy Saving Programme) Order 2009 and the Electricity and Gas (Carbon Emissions and Community Energy Saving) (Amendment) Order 2011.

- 1.4 The investigation arose following the submission of the final CERT report to the Secretary of State on 30 April 2013³, which provided details of the obligated parties' ("OP") achievements of the targets and obligations under the CERT programme, which finished on 31 December 2012⁴. The report sets out that British Gas did not comply with the targets set out in its CERT obligations.
- 1.5 The Authority noted that British Gas initially had an obligation to promote carbon savings equivalent to 96,279.607 kilo tonnes ("ktCO₂"). Under Article 9(1), as a group, British Gas delivered 98.9% of its overall CERT target and had a shortfall of 1,075.111 ktCO₂ at 31 December 2012. Under Article 9(1A), as a group, it delivered 95.5% of its Insulation Obligation target of 24,119.192 ktCO₂ and had a shortfall of 1,089.622 ktCO₂ at 31 December 2012. The shortfall of British Gas's overall CERT target was incurred entirely against its Insulation Obligation. British Gas accepts that it breached Articles 9(1) and 9(1A) of the CERT Order.
- 1.6 The Authority also noted that British Gas undertook mitigation action equivalent to the volume of its shortfall associated with not achieving the carbon reduction target promptly by February 2013 (for both the overall CERT obligation and IO) and had regard to this in setting the level of penalty.
- 1.7 The Authority has decided that British Gas breached Article 9(1) and Article 9(1A) of the CERT Order through having failed to achieve its carbon emissions reduction obligations by promoting qualifying actions to domestic energy users by 31 December 2012.
- 1.8 The Authority has decided it appropriate to impose a financial penalty on British Gas for the contravention of Article 9(1) and Article 9(1A) of the CERT Order, which occurred on 31 December 2012.
- 1.9 In the circumstances, the Authority has decided to impose a penalty of £1 on British Gas in respect of its failure to comply with Article 9(1) and Article 9(1A) of the CERT Order, on the basis that British Gas has made a payment of £500,000 (less the £1 financial penalty) in consumer redress to BGET on 27 February 2015. In deciding on the level of the penalty, which the Authority considers reasonable in all the circumstances, it took into account the following:
- (a) British Gas's failure to achieve the CERT target was a serious contravention of a major environmental programme;
 - (b) The extent of the initial shortfall in delivery of carbon reduction measures by British Gas was 1,075.111 ktCO₂ or 1.1% of its original obligation. Of its IO target British Gas had a shortfall of 1,089.622 ktCO₂ or 4.5% of its original obligation;

³ <https://www.ofgem.gov.uk/ofgem-publications/58425/certfinalreport2013300413.pdf>

⁴ Article 6(3) of the CERT Order provided that the obligation period for British Gas ended on 31 December 2012.

- (c) British Gas is unlikely to have made a significant net financial gain from the breach;
- (d) British Gas undertook mitigation action equivalent to the volume of the shortfall associated with its breach;
- (e) British Gas has one aggravating factor that partially applies (see paragraphs 5.13-5.17);
- (f) British Gas has several mitigating factors that apply (see paragraphs 5.21-5.24, 5.25-5.26, 5.29 and 5.31-5.33);
- (g) British Gas has agreed to settle this investigation; and
- (h) British Gas has made a payment of £500,000 (less the £1 financial penalty) in consumer redress as set out in paragraph 1.1.

In the judgement of the Authority, the aggregate of the penalty and the amount of consumer redress is a lower figure than would have been the case if British Gas had not taken the steps as set out in paragraphs (d) and (g) above, and the aggregate of the penalty and the amount of consumer redress is larger than the detriment suffered by consumers and the gain made by British Gas.

1.10 The penalty must be paid by 17 April 2015.

2 Background

The Carbon Emissions Reduction Target (CERT) Programme

- 2.1 The Carbon Emissions Reduction Target (CERT) was a policy, set down in legislation, designed to improve domestic energy efficiency standards across households in Great Britain. The policy was designed to contribute to the UK's legally binding emissions reduction commitments⁶. The relevant legislation was the Electricity and Gas (Carbon Emissions Reduction) Order 2008, as amended ("CERT Order").
- 2.2 Article 9(1) of the CERT Order required that certain gas and electricity suppliers must achieve their carbon emissions reduction obligations by promoting qualifying actions to domestic energy users in Great Britain. Article 9(1A) of the CERT Order required those suppliers to achieve a defined proportion of that obligation by promoting insulation measures. CERT placed an obligation on the six major electricity and gas suppliers (the obligated parties or 'OPs') to deliver specified amounts of carbon emissions reductions through qualifying measures.
- 2.3 The CERT obligation ran from 1 April 2008 to 31 December 2012 (referred to here as the 'compliance period'). Obligations under the CERT Order (including Articles 9(1) and Article 9(1A) referred to above) are relevant requirements for the purposes of the powers of the Authority to impose a

⁶ The UK government introduced a range of environmental policies to achieve a reduction of 80% in greenhouse gas emissions by 2050.

financial penalty for any failure to comply with such, under sections 27A Electricity Act 1989 and/or section 30A Gas Act 1986⁷.

- 2.4 The Department of Energy and Climate Change ("DECC") was responsible for drafting and implementing the legislation governing the scheme. This included setting the overall CERT target and those of the three CERT sub-obligations.⁸ Ofgem was responsible for administering the CERT programme, on behalf of the Authority.

British Gas's obligations under CERT

- 2.5 British Gas had an overall CERT obligation target of 96,279.607 ktCO₂. By 31 December 2012, British Gas had achieved 95,204.496 ktCO₂ of its obligation and was left with a shortfall of 1,075.111 ktCO₂ (shortfall of 1.1%).
- 2.6 British Gas had an Insulation Obligation (IO) target of 24,119.192 ktCO₂. By 31 December 2012, British Gas had achieved 23,029.570 ktCO₂ of its obligation and was left with a shortfall of 1,089.622 ktCO₂ (shortfall of 4.5%).

The Investigation

- 2.7 Ofgem takes compliance with all obligations seriously. When it became clear to Ofgem that there was a risk of non-compliance with CERT by several parties, Ofgem published an open letter dated 21 September 2012⁹, setting out its approach to enforcement in relation to CERT. This letter set out the way Ofgem and the Authority would approach actions taken by the OPs under CERT after the scheme's end date of 31 December 2012. The letter stated that Ofgem would take mitigation action into account in its enforcement procedures.¹⁰
- 2.8 Following the submission of the final CERT report to the Secretary of State on 30 April 2013 (see paragraph 1.3 above), Ofgem launched an investigation into British Gas. In particular, Ofgem investigated whether British Gas had met its carbon emissions reduction target and Insulation Obligation set out under the CERT order.

⁷ Please see section 41A(7A)(a) Electricity Act 1989, section 33BC(7A)(a) Gas Act 1986 and Article 23 of the CERT Order.

⁸ OPs were required to achieve the overall CERT target, and also separate targets for three sub-obligations: the Insulation Obligation (IO), the Priority Group (PG) and the Super Priority Group (SPG).

⁹ <https://www.ofgem.gov.uk/ofgem-publications/58765/open-letter-cert-cesp-210912.pdf>

¹⁰ Ofgem also published three other open letters:

- (i) on **20 December 2012**, setting out the administrative arrangements that Ofgem would use to process the mitigation actions delivered by OPs under CERT;
- (ii) on **31 January 2013**, setting out the way the Authority and Ofgem would approach the assessment and timing of mitigation actions taken by OPs under CERT; and
- (iii) on **29 May 2013**, setting out the administrative arrangements that Ofgem would use to process the mitigation actions delivered beyond 30 April 2013.

3 The Authority's decision on breach

- 3.1 Following an investigation by Ofgem into British Gas's compliance with the CERT Order, the Authority is satisfied that British Gas breached Article 9(1) and Article 9(1A) of the CERT Order.
- 3.2 Article 9(1) and Article 9(1A) of the CERT Order are relevant requirements for the purposes of section 27A of the Electricity Act 1989 (the Authority's power to impose a financial penalty)¹¹. Article 9(1) and Article 9(1A) mandated that British Gas achieve its carbon emissions reduction obligations by promoting qualifying actions to domestic energy users in Great Britain.
- 3.3 British Gas failed to achieve, by 31 December 2012, its carbon emissions reduction obligations mandated under Article 9(1) and Article 9(1A) of the CERT Order. It delivered 95,204.496 ktCO₂ and had a shortfall of 1,075.111 ktCO₂ against its overall CERT target of 96,279.607 ktCO₂. It delivered 23,029.570 ktCO₂ and had a shortfall of 1,089.622 ktCO₂ against its IO target of 24,119.192 ktCO₂.
- 3.4 This failure is evidenced by the Authority's report to the Secretary of State in April 2013 in which the Authority set out the levels of carbon emissions reductions achieved by OPs and whether they had met their obligations. British Gas does not dispute that the breach occurred.
- 3.5 In light of the finding of breach, the Authority considered whether to impose a financial penalty, under section 27A of the Electricity Act 1989 and/or section 30A of the Gas Act 1986.

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 considered whether a financial penalty is appropriate in accordance with the requirements of the Electricity Act 1989 and/or the Gas Act 1986 and having regard to its published Statement of Policy with respect to Financial Penalties (October 2003) ("the Penalties Policy").¹²
- 4.2 The Authority is required to take a decision on penalty in the manner which it considers is best calculated to further its principal objective¹³, and having regard to its other duties.

¹¹ See footnote 7.

¹² <https://www.ofgem.gov.uk/ofgem-publications/74207/utilities-act-statement-policy-respect-financial-penalties.pdf>

¹³ The Electricity Act 1989 (section 3A) and the Gas Act 1986 (section 4AA) set out details of the Authority's principal objective, as being the protection of the interests of existing and future consumers, wherever appropriate by promoting competition, and including their interests in the reduction of greenhouse gas emissions and the ensuring of the security of energy supply.

- 4.3 In deciding that it would be appropriate to impose a penalty, the Authority considered and took into full account the particular facts and circumstances of the contravention under consideration, including the extent to which the circumstances from which the contravention or failure arose were outside the control of British Gas. It also took full account of the representations made to it by British Gas.

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

- 4.4 The Authority considered that British Gas's breach of Article 9(1) and Article 9(1A) of the CERT Order damaged the interests of consumers in that energy efficiency measures were not installed in people's homes by the end of the CERT compliance period. Whilst British Gas was installing energy efficiency measures as mitigation action from January 2013, it took until February 2013 (by contrast to the 31 December 2012 deadline for substantive compliance) to deliver all of the expected energy efficiency measures, meaning energy savings for some consumers were delayed.¹⁴
- 4.5 The delay had a material impact on consumers, who experienced a particularly cold winter during the months of January and February 2013, with average temperatures below the long-term average from 1981 to 2010.¹⁵ During this period, at the height of winter, the affected consumers are likely to have faced higher energy bills than would otherwise have been the case, and would have been less likely to be able to afford to heat their homes adequately.
- 4.6 During that cold winter, domestic consumers used more gas than during either of the previous two winters.¹⁶
- 4.7 Further, the Authority considered whether non-compliance damaged the interests of other market participants who complied with CERT. The Authority considered the evidence to be inconclusive but noted that the case does not turn on this point.
- 4.8 The Authority also considered the extent to which harm caused to consumers will have been offset by over-delivery of mitigation activities. We consider this further in paragraphs 5.31-5.33 below.

¹⁴ 50,095 CERT IO measures were delivered late by 19 February 2013 (including some which were installed in 2012), when British Gas completed mitigation of its compliance shortfall.

¹⁵ <http://www.metoffice.gov.uk/climate/uk/summaries/anomalygraphs>. The Met Office publishes data on 30-year averaging periods, for 1961-1990, 1971-2000 and 1981-2010. Thus, 1981-2010 is the most recent data-set.

¹⁶ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/266718/et4_1.xls

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

- 4.9 The Authority considered that imposing a financial penalty is likely to create an incentive to compliance and deter future breaches:
- (a) both generally, as the Authority considered compliance with mandatory deadlines to be very important and not imposing a penalty in this case would not create the right incentives around the need for regulated parties to comply with deadlines; and
 - (b) specifically, in relation to environmental programmes, to incentivise companies to comply in full and on time with future mandatory energy efficiency obligations such as the Energy Companies Obligations (“ECO”).

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

If the contravention is trivial in nature

- 4.10 The Authority did not consider that British Gas’s failure to meet its CERT obligation was trivial. The Authority noted that British Gas’s overall CERT shortfall as at 31 December 2012 was 1,075.111 ktCO₂, equivalent to 1.1% of its overall CERT obligation. The Authority notes that British Gas’s IO shortfall as at 31 December 2012 was 1,089.622 ktCO₂, equivalent to 4.5% of its IO. Furthermore, over 50,000 energy efficiency measures were installed by British Gas as mitigation action.¹⁷

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

- 4.11 There is nothing in the Authority’s principal objective and duties as set out in section 3A of the Electricity Act 1989 and section 4AA of the Gas Act 1986 that precludes 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

- 4.12 The Authority considered that the breach or possibility of a breach would have been apparent to a diligent licensee. Companies were given four years and nine months to deliver their full obligation and two years and five months to deliver their IO obligation, and were aware that a breach of

¹⁷ See footnote 14.

these obligations would occur if they did not meet their full obligations by 31 December 2012.

- 4.13 In this case, the review of the evidence showed that British Gas's senior management became aware of the risks to compliance from December 2011. Therefore, the Authority considered that the breach or possibility of a breach would have been apparent to a diligent licensee.

Conclusion

- 4.14 Having taken into account the factors set out in the Penalties Policy and the representations made by the company, the Authority decided that the imposition of a penalty was appropriate in this case.

5 Criteria relevant to the level of financial penalty

- 5.1 In accordance with Section 270(1) of the Electricity Act 1989 and/or Section 300(1) of the Gas Act 1986, the Authority may impose a financial penalty of up to 10% of the annual turnover of the relevant license holder. The Authority was satisfied that its penalty fell within the maximum statutory limit.
- 5.2 In deciding the appropriate level of financial penalty, the Authority considered all the circumstances of the case, including the amount of consumer redress in the sum of £500,000 (minus the £1 financial penalty) and the following specific matters set out in the Penalties Policy.

Factors which are first considered when determining the general level of penalty

The seriousness of the contravention and failure

- 5.3 The Authority considered that British Gas's breach of CERT was serious. Companies had four years and nine months to comply with their overall CERT obligation, and two years and five months to comply with their IO obligation. The Authority expects regulated parties to meet mandatory obligations, in full and on time.
- 5.4 British Gas incurred shortfalls of 1,075.111 ktCO₂ for the overall CERT obligation and 1,089.622 ktCO₂ for the IO target (see paragraph 1.4 above). Unmitigated, the shortfalls would have been detrimental to the social policy objective underlying the CERT obligation, which was to improve the energy efficiency of domestic households in Great Britain. The Authority also noted that unmitigated shortfalls would have been detrimental to the UK's commitment under the Climate Change Act 2008 to reduce carbon emissions by 80% by 2050 compared to 1990 levels.

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

5.5 The degree of consumer harm has been set out above (see paragraphs 4.4 to 4.8). Once British Gas had completed its CERT mitigation activities in February 2013, the period of consumer harm ceased.

The duration of the contravention or failure

5.6 The breach of the obligation occurred at the deadline on 31 December 2012 when British Gas did not comply with the targets set out in its CERT obligation. After this date, the breach did not continue although the effects of the contravention persisted for seven weeks afterwards, i.e., until British Gas's mitigation activities were complete.

The gain (financial or otherwise) made by the licensee

5.7 The Authority considered whether or not British Gas made a financial gain through not meeting its obligations by the statutory deadline.

5.8 The Authority noted that British Gas's IO mitigation costs appeared to be higher than the average of IO costs per tCO₂ secured in the final year of CERT by British Gas and other OPs. As a consequence, the Authority did not consider that British Gas was likely to have made a gain by delivering at lower cost in mitigation than the prevailing market rate in the final year of CERT.

5.9 However, the Authority considered that British Gas had made a small financial gain, on a time value of money basis, by delaying a proportion of its CERT IO expenditure into the mitigation period. By not investing in CERT IO delivery in a manner that would achieve compliance, British Gas would have been in a position to put the deferred expenditure to alternative use.

5.10 On balance the Authority considered that it was unlikely that there was a significant net financial gain, given the high costs of mitigation.

Factors tending to increase the level of penalty

Repeated contravention or failure

5.11 British Gas had not previously failed to meet an energy efficiency obligation. The Authority did not consider that this aggravating factor applies.

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

5.12 The breach of the obligation occurred at 31 December 2012, when British Gas did not comply with the targets set out in its CERT obligation. After this date, the breach did not continue although the effects of the breach continued for seven weeks afterwards. The Authority did not consider that this aggravating factor applies.

Involvement of senior management in any contravention or failure

5.13 From the review of evidence, the Authority considered that British Gas's senior management and the Board of Directors were involved in key decisions regarding the CERT delivery strategy. British Gas had reporting structures in place for CERT at multiple tiers of British Gas and the Centrica group. Updates were provided to senior management by the operational team, in the form of Monthly Business Reviews (MBRs), Quarterly Business Reviews (QBRs) and Quarterly Performance Reviews (QPRs).

5.14 In June 2011, British Gas senior management (BGX) considered a marketing plan for the second half of 2011. Within the marketing plan it was contemplated whether or not insulation should be offered to consumers on a "free 'under any circumstances'" basis. However, it was not until a much later stage in the compliance period that British Gas offered free insulation to all energy consumers in Great Britain, in August 2012 (ie over 14 months later).

5.15 An internal meeting involving senior management (BGX) took place on 20 October 2011, concerning the CERT programme. The meeting slides indicate that by this point in time, British Gas believed that it had "little chance" of reaching its CERT targets. Two important decisions were made at this meeting. The first concerned various options for the level of investment in CERT for 2012. The operational team outlined a range of investment options. The outcome was that the British Gas Executive decided in favour of the highest investment option¹⁸, and this was noted in the meeting minutes. The second decision taken regarded free insulation offers, in particular whether or not the free insulation offer should be extended to all households in Great Britain. The meeting minutes show that the British Gas Executive decided not to do this, but only to continue offering free insulation to British Gas customers. With respect to this and paragraph 5.14 above the Authority noted that it was envisaged that customers would contribute towards the cost of measures.

5.16 British Gas was able to buy an "unprecedented amount" of Self Gen carbon (ie carbon from contractors that generated their own leads for

¹⁸ In fact, British Gas did not subsequently spend this entire budget in 2012.

installations) from third parties in Q4 2012, the last quarter of the compliance period. However, the Authority noted that this was very late in the compliance period and was only possible because other parties had excess carbon.

- 5.17 Taking the above into account, the Authority considered that British Gas's senior management and the Board of Directors were involved in British Gas's failure to achieve its CERT compliance target by 31 December 2012 and this aggravating factor therefore partially applies.

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

- 5.18 British Gas has provided evidence to show that it had internal procedures/mechanisms in place to prevent contravention of CERT. Those internal mechanisms or procedures included:

- a) Clear management structures in place for the internal management of CERT;
- b) Regular reporting to senior management on the progress of CERT delivery, through the MBRs, QBRs and QPRs;
- c) Use of risk management tools, such as maintenance of risk registers and regular risk monitoring at senior management level; and
- d) Establishing 'British Gas New Energy' and 'British Gas Communities and New Energy' as the organisations responsible for delivering CERT.

- 5.19 Taking the above into account, the Authority did not consider that there is an absence of any evidence of internal mechanisms or procedures intended to prevent contravention or failure. The Authority did not consider that this aggravating factor applies.

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

- 5.20 The investigation found no evidence of any attempt to conceal the contravention from Ofgem. The Authority did not consider that this aggravating factor applies.

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

- 5.21 The Authority expected a licensee seeking to meet its CERT obligation to devise a plan capable of achieving delivery within the compliance period – i.e. before 31 December 2012. This delivery process should have been subject to appropriate management supervision.
- 5.22 The Authority considered there is evidence that British Gas took steps to secure compliance including:
- a) Re-structuring to form a new business unit ('British Gas Communities and New Energy'), and making significant business acquisitions including insulation installers and social housing services providers;
 - b) Monitoring its CERT delivery appropriately through monthly and quarterly business performance reviews, and project management tools such as risk registers and financial plans;
 - c) Introducing free insulation to 'dual fuel BG customers' in February 2011, and introducing free insulation to 'any customer' in August 2012; and
 - d) Purchasing all of the surplus CERT carbon that was available from other OPs, in late 2012.
- 5.23 The Authority considered that although British Gas took these steps, ultimately these steps were insufficient to secure delivery on time. However, there is evidence that there was management supervision and monitoring of the compliance strategy present.
- 5.24 In view of the reasons above, the Authority considered that this mitigating factor applies.

Appropriate action by the licensee to remedy the contravention or failure

- 5.25 As noted in Ofgem's Open Letter of September 2012, mitigation action is not a substitute for compliance with the carbon emission reduction obligations and obligated parties should not be able to benefit from non-compliance. However in considering mitigation actions, Ofgem said that "*we will give most weight to CERT/CESP measures that are delivered shortly after 31 December 2012*". Ofgem later stated in its January 2013

Open Letter that 30 April 2013 would be a key date for assessing the mitigation actions taken by the parties.

- 5.26 The Authority noted that British Gas undertook prompt mitigation equivalent to the volume of its shortfall associated with not achieving the carbon saving reduction target. This mitigation was completed promptly and also by February 2013, i.e., before the key date of 30 April 2013. The Authority also noted that British Gas delivered more than its shortfall as mitigation (see paragraphs 5.31-5.33 below). In light of this, the Authority considered that British Gas did take appropriate action to remedy the breach and that this mitigating factor applies to a significant extent in this case.

Evidence that the contravention or failure was genuinely accidental or inadvertent

- 5.27 British Gas has made representations that factors including a lack of consumer demand for insulation and a lack of supply capacity in the insulation market affected its ability to deliver the obligation by the due date. The Authority noted that OPs had over four years to secure compliance with the CERT scheme and there has been no evidence to suggest that British Gas's contravention was genuinely accidental or inadvertent. Accordingly, the Authority did not consider that this mitigating factor applies in this case.

Reporting the contravention or failure to Ofgem

- 5.28 The arrangements under the CERT Order were that the Authority was required to report in April 2013, to the Secretary of State for Energy and Climate Change, its determination as to whether OPs had achieved their carbon emissions reduction targets. This report was duly presented and the OPs were notified of its conclusions. The Authority therefore considered that this factor did not apply.

Co-operation with Ofgem's investigation

- 5.29 British Gas has responded to Ofgem's Information Requests on time and complied with Ofgem's investigations process. However, the Authority considered that this mitigating factor should only apply where cooperation has gone beyond what would be expected of any licensee facing enforcement action¹⁹. In this case, British Gas has additionally, in response to the Settlement Mandate put forward, accepted its breach and

¹⁹ See the Notice of decision to impose a financial penalty upon SSE for non-compliance with its obligations under conditions 23 and 25 of the Standard Conditions of the Electricity and Gas Supply Licences - <https://www.ofgem.gov.uk/sites/default/files/sse-penalty-notice.pdf>

agreed to settle the case at the earliest opportunity. This has achieved a speedier resolution and avoided additional spending of resource by the regulator. Accordingly, the Authority considered that this mitigating factor applies and the Authority imposed a lower penalty (when considered in aggregate with consumer redress) than it would otherwise have imposed.

Other Factors

5.30 It was the view of the Authority that the following additional factors tending to reduce the level of any penalty were relevant in this matter.

Over-delivery of CERT IO mitigation measures

5.31 British Gas delivered mitigation actions in excess of the level required to address the harm associated with its breach. The Authority recognised that this additional delivery by British Gas provided enduring benefits for those consumers who had received those measures.

5.32 At the same time the Authority was aware that in relation to CERT and CESP, compliant suppliers were able to carry forward part of any over-delivery of compliance actions into the ECO scheme albeit not necessarily on a pound for pound basis.

5.33 The Authority balanced both of these points and considered that a mitigating factor should apply and to a significant extent.

6 The Authority's proposed decision as to the level of penalty

6.1 Taking all of the above into account, which includes the representations or objections submitted in response to its proposed penalty, the Authority has decided to impose on British Gas a £1 Penalty on the basis that British Gas has made a payment of £500,000 (less the £1 financial penalty) in consumer redress to BGET on 27 February 2015. The Authority considers this penalty to be reasonable in all the circumstances of the case. In reaching this decision the Authority considered in particular the following:

- (a) British Gas's failure to achieve the CERT target was a serious contravention of a major environmental programme;
- (b) The extent of the initial shortfall in delivery of carbon reduction measures by British Gas was 1,075.111 ktCO₂ or 1.1% of its original obligation. Of its IO target British Gas had a shortfall of 1,089.622 ktCO₂ or 4.5% of its original obligation;
- (c) British Gas is unlikely to have made a significant net financial gain from the breach;
- (d) British Gas undertook mitigation action equivalent to the volume of the shortfall associated with its breach;
- (e) British Gas has one aggravating factor that partially applies (see paragraphs 5.13-5.17);

- (f) British Gas has several mitigating factors that apply (see paragraphs 5.21-5.24, 5.25-5.26, 5.29 and 5.31-5.33);
- (g) British Gas has agreed to settle this investigation; and
- (h) British Gas has made a payment of £500,000 (less the £1 financial penalty) in consumer redress as set out in paragraph 1.1.

In the judgement of the Authority, the aggregate of the penalty and the amount of consumer redress is a lower figure than would have been the case if British Gas had not taken the steps as set out in paragraphs (d) and (g) above, and the aggregate of the penalty and the amount of consumer redress is larger than the detriment suffered by consumers and the gain made by British Gas.

Annex:

Representations or Objections on the Proposed Penalty

Introduction

- 1.1 The Authority received six representations or objections in response to its proposed penalty. The points made by the respondents can be grouped into four areas:
- The level of proposed penalty was too low (see paragraphs 1.3 to 1.4)
 - The proposed Penalty Notice lacked transparency (see paragraphs 1.5 to 1.7)
 - Points in relation to consumer redress (see paragraphs 1.8 to 1.13)
 - Other matters (see paragraphs 1.14 to 1.15)
- 1.2 The Authority has considered carefully all of the representations or objections, and its responses in respect of these four areas are set out below.

The level of proposed penalty was too low

- 1.3 Two respondents submitted that the level of proposed penalty was too low. One respondent questioned whether the level of penalty sent a clear enough signal to all parties about the importance of complying on time and in full for future obligations.
- 1.4 For the reasons given in paragraphs 5.7-5.10, the Authority's judgement is that the level of penalty for British Gas is reasonable in all of the circumstances of the case, and addresses the seriousness of the contravention.

The proposed penalty notice lacked transparency

- 1.5 A number of respondents submitted that the proposed penalty notice needed a greater level of detail²¹ in order to enable respondents to comment meaningfully on the level of penalty and/or consider whether British Gas gained an unfair advantage from not complying.
- 1.6 The decision on financial penalty (and the prior proposed decision on financial penalty) has been taken by the Authority having regard to its Penalties Policy. This includes that the assessment of the appropriate level of penalty should be taken having regard to a number of factors (rather than as an arithmetical calculation). The Authority is satisfied that the

²¹ For example, the penalty notice should quantify each element of the proposed penalty and should state British Gas's 'mitigation costs'.

level of detail in this Penalty Notice (and that previously in the proposed Penalty Notice) is fair, consistent with the Penalties Policy and follows the statutory requirements²², namely that the Authority states in its Notice:

- (i) that it proposes to impose/has imposed a penalty and the amount;
- (ii) the relevant condition breached;
- (iii) the acts or omissions which in the Authority's opinion constitute the contravention or failure and the other facts which justify the imposition of a penalty and the amount proposed for such penalty; and
- (iv) the time period within which representations or objections may be made with respect to the proposed penalty/the penalty is required to be paid.

1.7 Further, the Authority believes that the level of detail in the proposed penalty notice was sufficient for external stakeholders to comment meaningfully.

Points in relation to consumer redress

1.8 A number of respondents made a number of points in relation to the consumer redress British Gas is proposing. These points are considered below.

1.9 As a preliminary matter, the Authority's role is to consider whether the penalty is reasonable in all the circumstances, which includes taking into account any consumer redress paid or to be paid. In this case, the Authority is satisfied that the aggregate of the penalty and consumer redress is reasonable.

1.10 Several respondents submitted representations requesting that they should receive redress monies. The Authority considered that it was for British Gas to choose its redress recipients subject to the funding meeting the objectives referred to in paragraph 1.1.

1.11 One respondent said that redress should be "hard" energy efficiency measures (that is, solid wall insulation and other energy efficiency measures as opposed to more general advice and support). Wherever possible the Authority will wish to see consumer redress aligned to the original harm. Accordingly, the Authority has required that any consumer redress pursue the objectives referred to in paragraph 1.1 of this Penalty Notice. This is consistent with the policy objectives of CERT. At the same time, the Authority requires that any consumer redress must not adversely interfere with the delivery of other energy efficiency schemes such as the Energy Companies Obligation (ECO), or create an unreasonable administrative burden for Ofgem.

²² In section 27A Electricity Act 1989.

- 1.12 The Authority is satisfied that British Gas's proposal is within the scope of this mandate. The Authority notes that the BGET will be able to fund suitable projects involving "hard" energy efficiency measures, in addition to those involving more general advice and support. Further, the Authority notes that British Gas undertook mitigation action substantially in excess of the volume of the shortfall associated with its breach meaning that the original CERT objectives have been met and additional "hard measures" have been installed in any event.
- 1.13 A number of respondents considered it inappropriate for British Gas to make consumer redress through the BGET. However, the Authority notes that British Gas has given a senior Board-level assurance that the redress payment will not displace existing charitable funding, and that the BGET will be open to suitable applications from organisations matching at least one of the objectives set out in paragraph 1.1 above. Further, the Authority would be concerned if British Gas sought to derive any inappropriate publicity benefits from the payment to the BGET. The Authority notes from due diligence conducted by Ofgem that the BGET has a satisfactory track record and that other safeguards will be put in place to protect consumers' interests as part of the redress package.

Other matters

- 1.14 One respondent raised the following additional points:
- (a) It raised concerns that a non-compliant supplier should not be able to receive any credit for CERT mitigation which had also been claimed by the supplier under the ECO;
 - (b) It stated that any redress proposals should not distort the ECO and/or Green Deal in such a way that would cause detriment to the compliant CERT and CESP OPs; and
 - (c) It asked for further information on the degree of the over-delivery in CERT mitigation that was actually achieved by British Gas, to understand the Authority's conclusion in respect of this that a mitigating factor should apply and to a significant extent.
- 1.15 Each of these points is taken in turn below:
- (a) Regarding the possibility of a non-compliant supplier submitting the same activity as both substantive ECO compliance and CERT mitigation, Ofgem has been unable to identify any duplicate measures based on its records.
 - (b) Regarding redress activities causing possible impacts on the ECO and Green Deal programmes, the Authority considers that the proposed redress activities are not on a scale that would cause any significant distortions to these markets.
 - (c) Regarding British Gas' over-delivery in CERT mitigation, this was equal to more than half of the amount of its CERT IO compliance shortfall. Therefore, the Authority decided that this mitigating factor should apply and to a significant extent.

Gas and Electricity Markets Authority

5 March 2015