

Notice of decision to impose a financial penalty pursuant to 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 Opus Energy Limited with reporting requirements under the Renewables Obligation

29 October 2012

1. Summary

- 1.1. The Gas and Electricity Markets Authority ("the Authority") has decided to impose a financial penalty on Opus Energy Limited ("Opus") following an investigation into Opus's failure to report accurate supply data under the Renewables Obligation ("the RO") for England & Wales and Scotland, as set out in legislation¹.
- 1.2. By 1 July each year, electricity suppliers are required to inform the Authority of the amount of electricity supplied to customers in England & Wales and Scotland during the previous obligation period (from 1 April to 31 March).
- 1.3. Ofgem's investigation concerned Opus's procedures for the reporting of electricity supply data under the RO and information misreported for the obligation period 2009-10.
- 1.4. The Authority found that:
 - Opus underreported the amount of electricity it supplied to customers in England & Wales and Scotland for the obligation period 2009-10 by 7.4%; and
 - This resulted in a financial gain for Opus (and a consequent loss to market participants) in the sum of £360,000.
- 1.5. Opus took and is continuing to take appropriate steps to achieve compliance with the RO, action to remedy the financial gain and resulting market impact caused by the misreporting and ensure future compliance with the relevant obligations. Opus demonstrated to Ofgem that it had revised its methodology for calculating electricity supply data for the purposes of RO reporting and made appropriate changes to its internal procedures.
- 1.6. The Authority considered it appropriate to impose a financial penalty on Opus. In doing so, the Authority gave significant weight to the action taken by Opus to provide redress, its agreement to settle the investigation and its co-operation with Ofgem during the settlement process.
- 1.7. On 18 September 2012, the Authority gave notice of its proposed penalty of £125,000 on Opus in respect of contraventions of the relevant requirements in the obligation period 2009-10.
- 1.8. No representations were received in response to the Authority's proposal. The Authority has therefore decided to confirm the penalty of £125,000 on Opus.
- 1.9. The penalty must be paid by **10 December 2012**.

¹ The Renewables Obligation Order 2009 and the Renewables Obligation (Scotland) Order 2009.

2. Background

- 2.1. Under the RO, electricity suppliers are required to source a proportion of electricity supplied to UK customers from renewable sources. This proportion increases from year to year and reached 9.7 Renewables Obligation Certificates ("ROCs")² per 100 MWh in England, Wales and Scotland for the obligation period 2009-10³.
- 2.2. An electricity supplier can meet its obligations under the RO by:
 - presenting the requisite number of ROCs to the Authority for each obligation period;
 - making a payment into the buy-out fund equivalent to the number of ROCs they are required to present; or
 - using a combination of the two methods, by presenting some ROCs and making a payment into the buy-out fund for any shortfall.
- 2.3. Buy-out payments are received by Ofgem and recycled, on a pro rata basis, to those electricity suppliers who presented ROCs towards meeting their obligations. For example, in the 2009-10 obligation period, the combined total RO for all suppliers amounted to 30,101,092 ROCs. Of that obligation, 71% was met by presenting ROCs and the rest by buy-out payments. As a result, Ofgem recycled £323,337,635 to suppliers, who received £15.17 for every ROC they had submitted ("recycle value" of a ROC).
- 2.4. The number of ROCs each supplier needs to present is calculated on the basis of how many MWh of electricity they supplied during the relevant obligation period. As such, the Authority relies on receiving accurate reports of the amount of electricity supplied to customers in England & Wales and Scotland from individual suppliers by 1 July following the end of each obligation period.
- 2.5. In October 2010, following receipt of Ofgem's annual supplier audit programme into compliance with the reporting requirements under the RO, Ofgem identified that it appeared that Opus had underreported the amount of electricity it supplied to customers in England & Wales and Scotland for the obligation period 2009-10 by 7.4%. This audit and subsequent correspondence with Opus led to concerns that Opus had breached the reporting requirements under the RO.
- 2.6. Opus accepted that the misreporting was caused by shortcomings in its methodology for calculating electricity supply data for the purposes of RO reporting and its internal procedures. In particular, Opus's practice was to submit its own view of supply volumes rather than relying on industry feeds and/or comparing its own view with the overall ELEXON⁴ settlement volumes. In addition, senior management failed to provide appropriate resources to the calculation and provision of supply data and failed to arrange for appropriate checking and supervision by senior management and/or external auditors.

² Renewables Obligation Certificates (ROCs) are issued by the Authority to operators of accredited renewable energy generating stations for the eligible renewable electricity they generate. Operators can then trade the ROCs with other parties, including electricity suppliers who purchase the renewable electricity generated by the operators. ROCs are ultimately used by suppliers to demonstrate that they have met their renewables obligation.

³ Schedule 1 of the Renewables Obligation Order 2009 and the Renewables Obligation (Scotland) Order 2009 respectively.

⁴ ELEXON delivers the Balancing and Settlement Code for the electricity industry.

- 2.7. Opus took appropriate steps to address the harm caused by its failure to comply with the relevant obligations and specifically the additional payments it would have been required to make to discharge its RO in obligation period 2009-10. Opus retired a total of 7,016 ROCs in respect of the obligation periods 2010-11 and 2011-12, with an estimated value of £360,000. This has addressed the harm caused to market participants (with interest) as a result of Opus's underreporting in the obligation period 2009-10.
- 2.8. Opus also demonstrated to Ofgem that it had made the following changes to its procedures for reporting under the RO:
- Use of a revised methodology for calculating electricity supply data, which is in line with Ofgem's recommended methodology⁵;
 - Reorganisation of the company so that responsibility for RO reporting now rests with the Finance department, with appropriate oversight from the Finance Director;
 - Formalised and documented internal procedures for RO reporting; and
 - An annual audit of its RO procedures, using external auditors.

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

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

- 3.1. The Authority considered whether a financial penalty was appropriate in accordance with the requirements of the Electricity Act 1989 and its published Statement of Policy with respect to Financial Penalties (October 2003) ("the Policy"). The Authority may impose a penalty on Opus in respect of contraventions in the obligation period 2009-10.
- 3.2. 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 further its principal objective, having regard to its other duties.
- 3.3. In deciding whether it was appropriate to impose a financial penalty, the Authority considered all the circumstances of the case including, but not limited to, the specific matters set out in the Policy. These matters are examined in detail 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

- 3.4. The Authority found that the interests of other market participants had been damaged as a result of the misreporting. Opus took appropriate action to address this.

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

- 3.5. Misreporting of regulatory information, including information used for the administration of the RO, by any regulated company is difficult for Ofgem to detect without expending considerable resources. Misreporting has the potential

⁵ Renewables Obligation: Guidance for licensed electricity suppliers (May 2012), Appendix 5 – Recommended methodology for calculating electricity supply data:
http://www.ofgem.gov.uk/Sustainability/Environment/RenewablObl/Documents1/RO%20supplier%20guidance%202012_FINAL.pdf

to cause considerable detriment to other market participants and consumers should it go undetected for a significant period of time. It is therefore important that regulated entities are deterred from misreporting and incentivised to put adequate systems, processes and procedures in place to ensure accurate reporting of regulatory information, including information that Ofgem uses for the administration of environmental programmes, such as the RO. The Authority considers that the imposition of penalties in cases where misreporting comes to light (such as in this case) is likely to have this effect.

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

If the contravention is trivial in nature

- 3.6. The Authority did not consider that Opus's contraventions of the reporting requirements under the RO were trivial due to both the scale of the misreporting and the Authority's reliance on accurate regulatory information, including information used for the administration of the RO, in order to carry out its statutory functions effectively.

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

- 3.7. There is nothing in the Authority's principal objective and duties that precluded 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

- 3.8. The Authority considered that a diligent licensee would have devoted sufficient resources to ensuring that it had adequate systems, processes and procedures in place to avoid such misreporting.
- 3.9. After consideration of the above, the Authority considered that it was appropriate to impose a financial penalty in this case.

4. Criteria relevant to the level of financial penalty

- 4.1. In accordance with section 27A(8) of the Electricity Act 1989, the Authority may impose a financial penalty of up to 10 per cent of the annual turnover of the relevant licence holder. Annual turnover is defined in an Order issued by the Secretary of State⁶ as the applicable turnover for the business year preceding the date of this notice. In the business year ending on 31 March 2012, Opus had a turnover of £207 million.
- 4.2. In deciding the appropriate level of financial penalty, the Authority considered all the circumstances of the case, including the following specific matters set out in the Policy.

Factors which are first considered when determining the level of penalty

The seriousness of the contravention and failure

- 4.3. The Authority considered that Opus's breach of relevant requirements under secondary RO legislation could be qualified as a serious one, as Ofgem relies on accurate information being submitted by licence holders to carry out its statutory

⁶ The Electricity and Gas (Determination of Turnover for Penalties) Order 2002.

functions and administer environmental programmes, including the RO effectively.

- 4.4. If Ofgem was unable to rely on the accuracy of information submitted by licence holders, it would need to devote more resources to monitoring work. This would lead to an increased burden on both Ofgem and licence holders, higher overall costs of gas and electricity, and an increased likelihood of inaccuracy in regulatory decision-making and administration of environmental programmes such as the RO.

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

- 4.5. Other market participants were harmed as a result of Opus's misreporting and its consequential under-payment into the buy-out fund for the 2009-10 period. However, the Authority was satisfied that Opus had taken action to address this in full.

The duration of the contravention or failure

- 4.6. Opus confirmed that the same procedures for reporting under the RO had been in place for a number of years prior to the misreporting coming to light. The Authority took this fact into account in assessing the seriousness of the offence.

The gain (financial or otherwise) made by the licensee

- 4.7. Opus received a financial benefit from not buying additional ROCs and/or making appropriate payments to the buy-out fund. There was also an element of avoided cost associated with Opus's failure to allocate adequate resources to ensuring its compliance with the reporting requirements under the RO.

Factors tending to increase the level of penalty

Repeated contravention or failure or a continuation of failure after being aware of the contravention

- 4.8. There has been no previous finding of breach of the RO reporting requirements by Opus. The Authority was satisfied that there was no continuation of the contravention after it was identified by Ofgem. Opus demonstrated to Ofgem that it had taken appropriate steps to revise its procedures for RO reporting and monitoring its compliance with the relevant obligations. As with all suppliers, Opus's future compliance with the reporting requirements under the RO will be assessed as part of Ofgem's general monitoring work and through its annual supplier audit programme.

The involvement of senior management in any contravention or failure

- 4.9. The Authority did not consider that senior management were involved in any deliberate actions in relation to the contravention. However, the Authority considered that implementing appropriate RO reporting and monitoring procedures was the responsibility of senior management at Opus. The Authority therefore took the view that the decisions taken by senior management in this area contributed to Opus's failure to comply with the reporting requirements under the RO.

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

4.10. The Authority considered that internal mechanisms to prevent contravention or failure were absent in this case. This is because Opus's senior management failed to provide appropriate resources to the calculation and provision of supply data and failed to arrange for appropriate checking and supervision by senior management and/or external auditors.

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

4.11. Opus did not attempt to conceal the failures in its methodology from Ofgem.

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

4.12. Opus took the following steps to secure compliance with the reporting requirements under the RO:

- Use of a revised methodology for calculating electricity supply data, which is in line with Ofgem's recommended methodology⁷;
- Reorganisation of the company so that responsibility for RO reporting now rests with the Finance department, with appropriate oversight from the Finance Director;
- Formalised and documented internal procedures for RO reporting; and
- An annual audit of its RO procedures, using external auditors.

Appropriate action by the licensee to remedy the contravention or failure

4.13. Opus took action to address the impact to other market participants by retiring a total of 7,016 ROCs in respect of the obligation periods 2010-11 and 2011-12.

Evidence that the contravention or failure was genuinely accidental or inadvertent

4.14. While there was no evidence that the contravention was wilful, the contravention or failure could not be regarded as genuinely accidental or inadvertent, as it was within Opus's control to allocate appropriate resources to ensuring its compliance with the reporting requirements under the RO.

Reporting the contravention or failure to Ofgem

4.15. Opus did not self-report the contravention to Ofgem. It was identified by Ofgem through its annual supplier audit programme.

Co-operation with Ofgem's investigation

4.16. Opus co-operated with Ofgem during the settlement process. Because Opus decided not to contest Ofgem's findings, Ofgem did not have to spend additional resources on issuing a statement of case and preparing for an oral hearing. The

⁷ Renewables Obligation: Guidance for licensed electricity suppliers (May 2012), Appendix 5 – Recommended methodology for calculating electricity supply data:
http://www.ofgem.gov.uk/Sustainability/Environment/RenewablObl/Documents1/RO%20supplier%20guidance%202012_FINAL.pdf

Authority also gave weight to Opus's willingness (and agreement) to settle the investigation.

5. The Authority's decision

- 5.1. On 18 September 2012, the Authority gave notice of its proposed penalty of £125,000 on Opus in respect of contraventions of the relevant requirements in the obligation period 2009-10.
- 5.2. No representations were received in response to the Authority's proposal. The Authority has therefore decided to confirm the penalty of £125,000 on Opus.
- 5.3. The Authority has decided to impose a financial penalty on Opus of £125,000 which it considers to be reasonable in all the circumstances of the case. The penalty is a lower figure than would have been imposed if Opus:
 - had not been willing to engage with Ofgem during the settlement process;
 - had contested Ofgem's findings; and
 - had not taken prompt action to address the harm suffered by other market participants.
- 5.4. The penalty must be paid by **10 December 2012**.

Gas and Electricity Markets Authority

29 October 2012