Approach to enforcement

Decision on revising our enforcement procedure and financial penalties policy

28 June 2018



About the Utility Regulator

The Utility Regulator is the independent non-ministerial government department responsible for regulating Northern Ireland's electricity, gas, water and sewerage industries, to promote the short and long-term interests of consumers.

We are not a policy-making department of government, but we make sure that the energy and water utility industries in Northern Ireland are regulated and developed within ministerial policy as set out in our statutory duties.

We are governed by a Board of Directors and are accountable to the Northern Ireland Assembly through financial and annual reporting obligations.

We are based at Queens House in the centre of Belfast. The Chief Executive leads a management team of directors representing each of the key functional areas in the organisation: Corporate Affairs; Electricity; Gas; Retail and Social; and Water. The staff team includes economists, engineers, accountants, utility specialists, legal advisors and administration professionals.

Our Mission	Value and sustainability in energy and water.
Our Vision	We will make a difference for consumers by listening, innovating and leading.

Our Values

Be a best practice regulator: transparent, consistent, proportional, accountable, and targeted

Be a united team

Be collaborative and co-operative

Be professional

Listen and explain

Make a difference

Act with integrity

Abstract

This paper sets out the changes to our enforcement procedure and financial penalties policy which we have decided to make following consultation earlier in the year.

The objective of the revised enforcement procedure is to create a transparent process which will provide operational certainty for industry whilst at the same time providing us with the capacity to tailor the process to suit individual cases. The final **Enforcement Approach and Procedure** is published alongside this document. A **flow chart** summarizing the new procedure is also published. Both come into effect immediately.

We have also reviewed our financial penalties policy to ensure it works effectively and in tandem with the revised enforcement procedure. The final **Financial Penalties Policy** is published alongside this document. It also comes into effect immediately.

Audience

This document is likely to be of interest to regulated companies in the energy and water industry, government and other statutory bodies and consumer groups with an interest in the energy and water industries.

Consumer impact

The amendments to our enforcement process bring us in line with other sector Regulators and provide reassurance to stakeholders that we are focused on legislative and licence compliance.

Contents

Introduction

Purpose of this document

1. Effective and timely enforcement is of vital importance in order to ensure customer protection in line with promoting functioning markets. We currently have a number of statutory powers to take enforcement action against a regulated company for a breach of licence or a failure to comply with specified legislation.

2. In that regard the Utility Regulator (UR) set out for consultation a number of changes we proposed to make to the Enforcement Procedure and to the Financial Penalties Policy. We received 11 responses to the consultation and these are published alongside this document.

3. The purpose of this document is to set out our final decisions on changes to the Enforcement Procedure and to the Financial Penalties Policy. The revised procedure is entitled Our Enforcement Policy Approach and Procedure and is published alongside this document together with a summary flow-chart of the procedure. The revised Financial Penalties Policy is published alongside this document.

4. For an explanation of the changes we consulted on in respect of the Enforcement Procedure and the Financial Penalties Policy, please see sections 3 and 4 respectively of the consultation published in February 2018.

Coming into effect

5. The revised Enforcement Procedure and the revised Financial Penalties Policy come into effect immediately.

Summary of responses to proposed changes to enforcement policy approach and procedure

6. This section summaries the responses to our consultation on the revised Enforcement Procedure. We also set out the changes to the procedure in consequence.

Aim of the revised enforcement approach and procedure

7. Some of the responses commented explicitly on the aim of the revised procedure. These either supported the revised aim or suggested that it could be expanded further to provide for protecting the industry and the competitive market, including the interests of suppliers and other market participants.

8. In regard to expanding the aim of the policy we consider this is not necessary as ensuring adherence to licence obligations (as is reflected in the aim of the enforcement procedure) will ensure a healthy functioning market and that this is the ultimate protection for the industry and the market participants within it.

9. One respondent argued that the aim of the revised procedure should be to ensure compliance rather than to incentivise compliance. However, the aim of ensuring compliance is consistent with the UR's powers under the Energy Order and Water Order. Under the Orders our powers relate to 'enforcement' of contraventions, and not merely to incentivising compliance.

10. One response also noted the importance of balancing deterrence and the desire to incentivise other companies to comply with best practice, with natural justice and the rights of the company under investigation (especially where an investigation

is ongoing). In this regard we note that our approach to investigating any potential contravention and making enforcement related decisions is designed to be rigorous, thorough, evidence-based and fair so as to ensure that the outcomes reached are proportionate and consistent. The process affords the company a right to input at various points.

Publicity

11. A range of views were expressed on the proposals on publication. These ranged from full support for the proposals to opposition to publication at each stage and questioning why the UR must consult on the penalty. Some of the responses opposed to publication cited the fact that publishing case details before the outcome of enforcement action was known could be detrimental to the reputational and other interest of regulated companies. In particular some of the responses were concerned about publication of alternative resolution outcomes at the initial enquiry stage. Other responses welcomed the clarity in the document with regard to publication, acknowledged the aim of increasing transparency to customers and stakeholders, and noted that this represented a best practice approach to enforcement and should act as a significant deterrent.

12. Some of the responses suggested that one day advance notice of what would be published on the UR website is too short and this period should be longer. Also that the UR should always inform the regulated company before publishing anything about their case on the website and any note published, e.g. at case opening stage should make it clear that this does not imply that the UR has made any finding about non-compliance.

13. We note the support expressed for our proposals on publication and in particular the acknowledgement that transparency is important and that publication should act as a significant deterrent. We have carefully considered the concerns raised by those not in favour at the various stages of the procedure. On balance we have concluded that the aims of transparency and accountability are supported by

publication and that this should act as a deterrent and incentivize best practice more generally. We have therefore not changed our proposals on publication except in regard to alternative resolution outcomes at the initial enquiry stage.

14. These will not be published on our website as a news alert but will be published later in a UR publication such as the Annual Report, see paragraph 2.7 of the enforcement procedure.

15. For information on when we will publish information and what will be published at each stage of the procedure, see Sections 3 and 4 of the enforcement procedure and in particular paragraphs 3.23, 4.14, 4.46, 4.55, and 4.57.

16. In regard to the notice given when we publish an outcome on the UR website, we consider that one day notice is sufficient as the copy of the publication is for information only. We have amended the procedure to indicate that we will inform the company in advance (see paragraph 2.9).

17. It should be noted that in the event of a case settled by agreement the company will have advance sight of the draft penalty notice and draft press release. We will seek to reach agreement with the company on the penalty amount that will appear in the penalty notice. The company will also have an opportunity to comment on the content of any draft press notice but the final decision as to what will be published in the press notice will be made by the UR. We have made changes to the Enforcement Procedure to clarify the engagement with the company during this aspect of the process (see paragraph 4.25).

18. In addition we have added drafting to the Enforcement Procedure to make it clear that when we publish a notification on our website that we have formally commenced an enforcement, we will make it clear that this does not imply that we have made any findings about non-compliance (see paragraph 4.14).

Prioritisation principles

19. There was general support in the responses for the use of prioritization principles.

20. Some of the responses requested that the principles should be included in the procedure for transparency, or suggested that they could be expanded further. Also that the principles should not be limited as there may be other principles that could apply in a specific case. One response noted that the principles do not appear to take account of a situation where a licensee may have proactively raised an issue with the UR.

21. We have amended the procedure to include the prioritization principles below (see paragraph 2.14). We agree that this list is not exhaustive and other principles may apply depending on the nature of the case.

- the likely impact of the investigation in terms of the direct and indirect consumer benefit that investigation may bring;
- the significance of the case (including strategic fit, the seriousness of the contravention, the level of harm to consumers, the duration of the contravention);
- whether other tools are available that would be more appropriate to achieve the same or a better outcome;
- the resources required to carry out the investigation and the availability of such resources;
- whether taking enforcement action could deter contraventions in the future, including whether the case will have a more general deterrent effect; and

- whether we are the most appropriate body to carry out a formal investigation or whether another body is better placed, is already carrying out or has already carried out such an investigation.

22. Regarding whether the principles should take account of a situation where a licensee may have proactively raised an issue with the UR. We do not agree that this should be considered as a prioritisation principle. We may open a case even where a licensee has been proactive in reporting as breach because we may consider, for example, the conduct in question to have caused serious harm to consumers or where we consider the investigation could bring other consumer benefit. Whether the licensee has proactively raised an issue with the UR is considered as a mitigating factor in the context of the Financial Penalties Policy.

23. One response asked for clarity on how, in the context of considering the significance of a case, the level of harm to consumers will be quantified. In applying the prioritisation principles we do not anticipate that customer harm will be quantified in monetary terms. But we will take into consideration, for example, the number of customers involved and any evidence available as to the extent of harm that may have been caused to them.

24. One response suggested that the UR should have an overarching obligation to include, for example, the need to outline any concerns UR may have in terms of a potential or actual contravention of any legislative or licence obligation, to assess whether the party has acted in a reasonable manner given all its duties and responsibilities, and ensuring sufficient and reasonable time for any resolution to be given effect.

25. In regard to the need for an overarching obligation, many of the aspects outlined above relate to ensuring the fairness and transparency of the procedure and so we have not included any specific drafting to cover these in the prioritization principles. We consider that our approach to investigating any potential contravention

and making enforcement related decisions is already designed to be rigorous, thorough, evidence-based and fair so as to ensure that the outcomes reached are proportionate, transparent, and consistent. The process also provides for the licensee to comment on the UR's thinking at various stages.

26. The same respondent also suggested that the prioritisation principles should provide for consideration of the potential damage any investigation and/or enforcement action could have on a licenced company and its ability to continue to operate as a viable entity in the market, where such continuation is in the best interests of consumers. We do not agree that a principle along these lines would strike the correct balance given that the enforcement process aims to ensure that we protect the interests of consumers and to secure that regulated companies comply with their obligations.

Alternative resolution

27. All the responses who commented on alternative resolution specifically supported the inclusion of alternative resolution in the Enforcement Procedure.

28. However, some wished to see changes to the alternative resolution process such as:

a) Alternative resolution should be considered in all cases and must be available throughout the entire process, including after the Summary of Initial Findings (SIF) has been issued;
b) Alternative resolution discussions a 'without prejudice' basis;
c) The application of the prioritization principles to determine if a case is suitable for alternative resolution is unnecessarily restrictive;
d) The second step in the initial enquiry stage to provide for a licensee without prejudice to hear the allegations being made and an opportunity to respond and challenge before a decision is made to proceed.

29. We have considered all the changes proposed to the alternative resolution

process in the responses. In regard to a) above, the procedure makes ample provision for the company to propose alternative resolution both at the Initial Enquiry Stage and during Enforcement Action Stage I. However, ultimately alternative resolution must be agreed by the UR and where it does not so agree (and the case is not otherwise closed) the only alternative is enforcement action proceeding.

30. In regard to whether alternative resolution discussions should take place on a 'without prejudice' basis, we do not consider that this is necessary. Alternative resolution, if agreed, will entail no admission of breach and instead the UR agrees that the alternative resolution offered is more appropriate than a full enforcement process

31. We do not agree that the application of the prioritization principles to determine if a case is suitable for alternative resolution is unnecessarily restrictive. The principles listed in the Enforcement Procedure are not exhaustive.

32. We have made some amendments to the procedure at 4.8 to make it clear that during the Initial Enquiry Stage we envisage that there will be informal discussions with the company such that the company will be aware of the issues under consideration and have a chance to respond to them.

33. Some of the responses posed questions or sought further clarity about aspects of the alternative resolution process set out for consultation. As a consequence we wish to provide the following clarification:

a. There is a general presumption of compliance until it can be demonstrated otherwise;
b. A licensee can break off alternative resolution discussions and subsequently decide to contest a case;
c. We encourage companies to offer alternative solution proposals but proposals will not be automatically accepted. The enforcement procedure sets out what proposals should contain and what the UR will

consider in evaluating them (see paragraphs 3.19 and 3.20). Alternative resolution will not be suitable in all cases and are likely to be most appropriate in cases in which it would be a more proportionate way of responding to the contravention while still effectively protecting the interests of consumers and of the market, and deterring future contraventions;

d. A case closed by means of alternative resolution does not mean the company is cleared of wrong-doing, in such cases there is no formal finding one way or the other;
e. We agree that alternative resolution proposals must provide comprehensive assurances that the matter has been addressed, including compensation for customers and meaningful measures to demonstrate a commitment to preventing future contraventions.

Settlement of cases

34. All the responses supported the inclusion of a settlement process in the enforcement procedure.

35. However, some wished to see changes to the settlement process such as:

a. different discounts (either higher or lower), or that the degree of discount should not be related only to how early a settlement agreement is signed;
b. a small number of responses advanced the idea that industry participants, including suppliers, to be represented on the settlement/enforcement committee;
c. that companies who settle should be able to admit a breach without having to admit to others and give up its right to appeal; and
d. one response stated that it was unnecessarily onerous to insist that a party must admit to contraventions under investigation.

36. In regard to the level of the discount, one response stated that the discounts

should be 50% and 30% and another response that the discount in the first window should be 30%. A further response argued that flexibility should be allowed at the second window to alter the discount upwards – potentially to 40%. Other responses support the proposal consulted on. Given that many responses support the UR's proposal on discounts while the rest of the responses evidence a range of views on the level of the settlement discounts, the final decision does not change the proposal consulted on. However, we will keep the level of discounts under review as we use the policy to ensure that they are proportionate to the administrative savings from early settlement.

37. In regard to the idea that suppliers, other industry participants or a third party should be represented on a settlement/enforcement committee; the purpose of the settlement or enforcement committee is to perform a function of the UR (its enforcement function), therefore either committee can only be comprised of any member or employee of the authority who is authorised for that purpose. See the Energy (NI) Order 2003, Schedule 1(9).

38. In regard to the proposal that settlement entails an admission of breach and that a company gives up its right of appeal; settlement is distinct from alternative resolution and entails an admission of breach in order to settle the case as without such an admission and signed settlement agreement the subsequent process cannot be streamlined and settlement has no value. If the company does not give up its right of appeal the benefits from settlement may be undermined – an appeal would lead to an expensive and protracted process which is what settlement would avoid.

39. Some of the responses also posed questions or sought clarity about aspects of the settlement process. As a consequence we have made a number of changes to the Enforcement Procedure for clarity.

40. We will consider a case as contested after window one on a preliminary basis.

41. Settled cases will proceed for decision to the settlement committee (see

paragraph 4.29).

42. Where a settlement agreement is not signed in the first window, the company will have a duration of the second window to sign an agreement if it wishes to do so (see paragraph 3.30 and 4.36).

43. The amount of the financial penalty will be known to the company before it agrees to settle as it will be contained in the draft penalty notice. We have added drafting to 4.25 to make it clear that the aim of the settlement discussions will be to agree the penalty amount contained in the draft penalty notice.

44. Once the settlement agreement has been signed the Utility Regulator will not revisit the penalty unless this becomes necessary by virtue of the statutory consultation on the financial penalty (see drafting added in paragraph 3.31).

45. We have added drafting at 5.6 to clarify that the same single person cannot be a member of both the enforcement committee and the settlement committee. If no settlement is agreed and an enforcement committee is formed, the enforcement committee will have members who have not been involved in any deliberations about the case previously, i.e. not been part of the investigation team or the settlement committee. This means they will be able to consider the issues afresh. In order to safeguard the integrity of the process they will not see any admissions made by the company in the settlement discussions. In considering the issues afresh, the enforcement committee will not be bound by any draft penalty notice previously shared with the company.

46. We have made some changes to section 5 of the procedure to ensure that the drafting here applies equally to the enforcement and the settlement committee, for example in regard to the establishment and membership of these committees. Also we have made some changes to paragraph 5.2 to clarify our intent as to the number of members on a committee and to delete the reference to either committee comprising the full UR board. Membership of either committee is decided by our Chair and the company will be able to make representations on the make-up of the enforcement and the settlement committee (paragraph 5.3).

Other comments

47. Some of the other comments or requests for clarity that do not fall within the subject headings above are highlighted below.

48. Two responses asked for information on the appeals process. We do not consider that this needs to be set out in the procedure. In any case the recourse for companies that are aggrieved by decisions of the UR in respect of financial penalties is set out in the Energy Order – see Article 49(1) of the Energy Order. See also paragraph 58 below.

49. Some of the responses requested either more defined timescales (e.g. a backstop timeline) or more flexible timescales. Individual cases may vary significantly therefore we consider that it is not appropriate to put in place a rule for how much time we will take to resolve cases. Also, in regard to timescales for responding to information requests, the draft SIF, and draft Statement of Case, for the same reason it is also necessary to retain flexibility.

50. We have made slight amendments to paragraph 1.7 to clarify that the enforcement procedure does not apply in respect of matters or decisions that are within the jurisdiction of the SEM Committee in relation to the all-Ireland Single Electricity Market.

51. One response noted that Ofgem's enforcement guidelines include a section on self-reporting which refers to reporting of 'potential breaches that may give rise to material harm to consumers, the market or Ofgem's ability to regulate,' and suggested that the UR's creates guidance on self-reporting to ensure that the most impactful or material issues are raised.

52. We consider that it is for the company concerned to decide what it wishes to report to the UR. Also, given that competition is at an earlier stage of development in NI compared to GB and the market is much smaller here, we do not think that the UR

should indicate a threshold for what ought to be reported to the UR. We also consider that Ofgem's guidance is framed more widely than presented in the response. Consequently, our view is that guidance on self-reporting is not necessary.

53. One response suggested that throughout the process due regard should be taken of the reasonable right and expectations of such licensed companies to make a reasonable return and to be able to finance their activities. In this regard we note that the UR's duties around financibility are not expressed in this way but instead relate to whether or not a company can finance the obligations placed on it.

54. One response sought clarification with regard to why the UR may need a non-confidential version of any documents submitted. Paragraph 2.10 of the procedure now states that where information is provided to us via a complaint from a third party (which could include another licensee) or a whistle-blower, we may need to disclose that information either to the company under investigation or to others connected to the subject matter of the complaint. Where information is confidential or where a complainant does not wish it to be disclosed, this should be made clear, including the reasons why, in writing.

55. One respondent requested clarification with regard to the procedure for a provisional enforcement order and whether there are provisions for compensation or restitution should a licence breach not be proved. Following the enforcement procedure in full is unlikely to be suitable for cases where the UR considers it appropriate to make a provisional order. This is because a provisional order can be made where the UR considers it needs to take action quickly (effectively on an urgent basis) because the breach/likely breach means that a third party is likely to sustain loss or damage as a consequence of anything done or not done by the company before a final order can be made. In these circumstances it would not be appropriate for either any or all of the stages set out in the enforcement procedure to be followed. In these circumstances the UR will adopt such a procedure as it considers would be appropriate given the particular circumstances of the case and the particular reasons for the need to make a provisional order.

56. There are no provisions for compensation or restitution in cases where the UR takes enforcement action. That is not to say there is no recourse for companies that are aggrieved by the order and wish to question the validity of any order made or confirmed by the UR – see Article 44(1) of the Energy Order.

Enforcement Procedure – flowchart

57. One respondent commented on the flow-chart in particular. We have revised the flow chart and made some amendments to it for clarity and to ensure that the stages of the process are clear and distinguishable from each other.

58. In this regard we have found it helpful to split the final stage in two. For this reasons the flowchart and the procedure now list four stages and these are listed at paragraph 3.3 in the procedure and explained thereafter.

Summary of responses to proposed changes to UR's financial penalties policy

59. There was general support for the changes proposed to the Financial Penalties Policy.

60. One response asked for clarification on customer redress within the calculation of the penalty, particularly in light of the legislative requirement to pay sums received into the Consolidated Fund.

61. In this regard we have made changes to step 4 (the application of the settlement discount) to indicate that the means of redress will be agreed with the company as part of the settlement agreement. Where the company agrees to make a monetary payment as a form of consumer redress, that amount shall be deducted from the amount of the financial penalty that would otherwise have been imposed by the Utility Regulator which may result in the financial penalty itself being of a nominal amount. Also that in accordance with the applicable statutory provisions, any amount received by the Utility Regulator by way of a financial penalty which is ultimately imposed on the company (which for these purposes does not include any amount which the company pays in the form of customer redress) shall be paid into the Consolidated Fund.

62. We have also made amendments to the policy to remove references to customer redress from the explanation of step one (the calculation on gain and detriment) and consider that this section is clearer as a result as it now focused only on this calculation.

63. One response asked why the amended financial penalties policy gives more prominence to gain/detriment. This was explained in paragraph 66 of the consultation document. The assessment of gain and detriment is applied by other regulators, see

for example the Ofgem policy on Financial Penalties.[1]

64. One respondent set out its understanding in regard to the liability of the vertically integrated utility (VIU) and what this relates to (unbundling requirements and associated obligations in Directive 2009/72/EC. The response requested that the UR confirm the understanding set out and provide additional guidance in relation to the type of situation whereby a penalty may take the licensees position as part of a VIU into account.

65. Paragraph 1.2 of the FPP indicates that where the regulated person is or is part of a vertically integrated undertaking and the relevant condition or requirement to which the contravention relates is imposed on a vertically integrated undertaking pursuant to the Electricity Directive (2009/72/EC) or the Gas Directive (2009/73/EC), a penalty imposed shall not exceed 10% of the turnover of the vertically integrated undertaking. We consider that whether a company is part of a VIU will be a matter of fact and the UR will apply the legislation to each individual case.

[1] https://www.ofgem.gov.uk/sites/default/files/docs/2014/11/financial_penalties_and_consumer_redress_policy_statement_6_november_2014.pdf