


Consultation on a proposed new power for Ofgem to compel regulated energy businesses to provide redress to consumers

DECC consultation document



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Foreword / Introduction

In the context of the rises in energy prices we have experienced over recent times it is crucial that consumers are both able to find the best deals and are treated fairly. There are already strong rules in place to protect consumers and Ofgem is currently consulting on a number of measures which will simplify tariffs and make it easier for consumers to engage in energy markets with confidence. The Government supports the action the regulator is taking but we also want to ensure that Ofgem has the powers it needs to obtain fair outcomes for consumers when they suffer a loss because energy businesses fail to meet their obligations under energy legislation.

In certain circumstances, Ofgem can and does impose substantial fines on businesses for breach of their regulatory obligations. But the Government believes that where individual consumers have suffered a direct loss as a result of such breaches the ideal remedy should be compensation. When Ofgem investigates an alleged breach it is well-placed to establish whether any consumers have suffered a loss and whether compensation is appropriate. It regularly negotiates with businesses to obtain compensation for consumers but there is currently no obligation on businesses to provide

redress and no formal mechanism by which Ofgem can make them do so. This consultation sets out the Government's proposals to give Ofgem this power and thereby increase the likelihood of consumers receiving redress when they suffer a loss as a result of a regulatory breach.

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General information

Purpose of this consultation

Set out what Government is trying to achieve with the consultation and in particular whose views it is seeking.

Issued: 10 April 2012

Respond by: 2 July 2012

Enquiries to:

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Consultation reference: URN 12D/060 – Consultation on a proposed new power for Ofgem to complete regulated energy businesses to provide redress to consumers

Territorial extent:

England, Scotland and Wales.

How to respond:

Your response will most useful if it is framed in direct response to the questions posed, though further comments and evidence are also welcome. We would be happy to accept responses in either written or electronic form.

Additional copies:

You may make copies of this document without seeking permission. An electronic version can be found at

http://www.decc.gov.uk/en/content/cms/consultations/ofgem_redress/ofgem_redress.aspx

Other versions of the document in Braille, large print or audio-cassette are available on request. This includes a Welsh version. Please contact us under the above details to request alternative versions.

Confidentiality and data protection:

Information provided in response to this consultation, including personal information, may be subject to publication or disclosure in accordance with the access to information legislation (primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

If you want information that you provide to be treated as confidential please say so clearly in writing when you send your response to the consultation. It would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded by us as a confidentiality request.

We will summarise all responses and place this summary on our website at www.decc.gov.uk/en/content/cms/consultations/. This summary will include a list of names or organisations that responded but not people's personal names, addresses or other contact details.

Quality assurance:

This consultation has been carried out in accordance with the Government's Code of Practice on consultation, which can be found here:

<http://www.bis.gov.uk/files/file47158.pdf>

If you have any complaints about the consultation process (as opposed to comments about the issues which are the subject of the consultation) please address them to:

DECC Consultation Co-ordinator
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Executive Summary

Gas and electricity businesses are subject to a range of obligations set out in or deriving from legislation. Failure to comply with some of these obligations can trigger enforcement action by Ofgem, including a fine of up to 10% of annual turnover. The sub-set of obligations enforceable in this way are referred to here as “relevant obligations”.

In some cases, non-compliance with relevant obligations will have led to consumers suffering a financial loss. As a result of Ofgem’s enforcement action, consumers may be able to take individual action to seek redress but this will depend upon their willingness to do so and whether they have a cause of action, such as breach of contract. When Ofgem investigates a breach of a regulatory obligation, it will seek evidence of the extent of the harm to consumers and so it is well-placed to identify whether redress is appropriate and what form this should take. Ofgem sometimes seeks to reach a voluntary agreement with businesses and has been successful in obtaining redress, including monetary compensation for consumers. However, there have also been occasions when it has been unsuccessful in reaching a voluntary agreement and, as it has no powers to compel redress to be provided, consumers will have missed out on redress that might have been due to them.

The Government is proposing that Ofgem should be provided with a power which would enable it to order an energy business to remedy the adverse effects on consumers of a breach of a relevant obligation. We would still expect voluntary agreements on redress to be the norm but the proposed power would strengthen Ofgem’s hand during negotiations and also give it a means of ensuring consumers are compensated where energy businesses are unwilling to provide this voluntarily.

Redress orders could require consumers to be compensated on a “pound for pound” basis where consumers have suffered a measurable loss, good will payments where it is not easy to determine the extent of the loss and public apologies or other remedies. Ofgem would have discretion to determine what form of redress is appropriate.

This consultation invites views on the scope of the proposed power in terms of the range of remedies and whether others as well as consumers should be eligible for compensation.

Catalogue of consultation questions

Consultation Question	
1.	Do you agree that Ofgem should be able to order an energy business that is in breach of relevant obligations to make appropriate redress to consumers who have suffered a loss as a result of the breach?
Consultation Question	
2.	Do you agree that Ofgem should be able to compel both licensed and licence-exempt energy undertakings to provide redress when they breach relevant obligations?
Consultation Question	
3.	Do you agree that Ofgem should be able to order compensation to be paid to other market participants, not just individual consumers?
Consultation Question	
4.	Do you agree that Ofgem should have discretion to decide what form of redress is appropriate to address the detriment caused by regulatory breaches?
Consultation question	
5.	Can energy businesses provide us with information about the administrative or other costs they anticipate they might face should Ofgem require them to provide redress to consumers?

Proposed new redress power for Ofgem

Introduction

1. Ofgem is the GB independent regulator for gas and electricity markets. Its principal objective is to protect the interests of consumers and it does this by administering the gas and electricity licensing regime and enforcing other relevant obligations¹ with which businesses operating in these sectors are required to comply.
2. Ofgem can take enforcement action against an energy business which does not comply with a relevant obligation. It can impose a fine up to 10% of the business's annual turnover. Fines can therefore be substantial and act as both an effective punishment and deterrent.
3. However, in some cases where energy businesses have breached a relevant obligation, its customers, whether domestic consumers or other businesses (and possibly also third parties²), will have suffered a financial loss. Consumers may be able to seek compensation by taking individual action in the courts (where they have a cause of action such as breach of contract) or refer their cases to the Energy Ombudsman, but many of them will not do so.
4. When Ofgem investigates an alleged breach of a relevant obligation, it will often assess the impact on consumers in order to determine the extent of the harm the breach may have caused and the level of the appropriate penalty. Any financial losses that consumers have suffered as a result of being overcharged for their energy, for example, will be factors for consideration. Where Ofgem is able to determine the financial loss suffered by consumers it will be in a good position to identify the appropriate level of redress, including monetary compensation, but it has no powers which it can use to compel compensation to be paid.
5. Where Ofgem is satisfied that a business has breached or is breaching a relevant obligation, it is able to impose a penalty of such an amount as is reasonable in the circumstances of the case. In determining what is reasonable, Ofgem takes account of whether appropriate action has been taken to remedy the contravention or failure and, where it has, may impose a smaller fine than would otherwise have been the case. This can act as an informal lever which helps it to negotiate redress on behalf of consumers. However, as Ofgem cannot either compel businesses to offer redress or distribute the fines it levies to consumers, there is no guarantee that this will be provided.

¹ The relevant legislation is the Electricity Act 1989 and the Gas Act 1986. A business's relevant obligations depend on what function it performs (e.g. electricity generator or gas transporter) and whether or not it holds a licence under the Electricity Act 1989 or the Gas Act 1986 to do so. A licensed business's relevant obligations are made up of its licence conditions and other statutory obligations for the type of business it is in Schedule 6 of the Electricity Act 1989 or Schedule 4B of the Gas Act 1986; those of non-licence holding businesses ("exempt" operators) are simply as specified in the Schedules.

² For example, if the business in breach of a relevant obligation is an electricity generator, not only its direct customers (energy suppliers) but also their customers (domestic and other consumers) may be affected.

6. The Government believes that providing Ofgem with a formal power to order companies to make redress in certain circumstances would strengthen Ofgem's ability to protect the interests of consumers and increase justice and fairness in energy markets by requiring companies to put right the effects of their wrongdoing rather than simply pay a fine.

Regulatory framework and Ofgem's current enforcement powers

7. Unless it is exempt, any undertaking wanting to supply gas or electricity to customers, or operate a gas or electricity network or an interconnector or generate electricity has to be licensed by Ofgem. In addition to complying with general consumer protection and competition law, licensees are required to comply with a series of licence conditions and other relevant obligations. These include important safeguards for consumers, such as rules on sales practices, providing connections and complaints handling. In addition, both licensees and other gas and electricity businesses which are not required to hold a licence ("exempt undertakings") have to comply with relevant obligations, covering matters such as third party access to distribution networks, how long a supplier takes to switch customers to another supplier and information requirements.

8. Ofgem monitors energy businesses to ensure that they abide by these relevant obligations and can investigate if it has reasons to suspect that they may be in breach of them. If it finds that a breach of a licence condition or other relevant obligation has occurred, it has the power to issue an order which requires the business to take action to stop the breach and bring itself back into compliance. It can also impose financial penalties of up to 10% of the company's annual turnover. These fines can be substantial. During the past three years, Ofgem has imposed fines on licensees totalling £3m for not meeting relevant obligations in relation to providing connections, £9m for failing to meet reporting requirements and £1.8m for misselling.

9. Currently, Ofgem has no power to compel compensation to be paid to consumers even when it can be clearly demonstrated that they have suffered a loss as a result of the breach. The monies from fines it imposes are paid into the Consolidated Fund, the Government's general bank account. Individual consumers do have a right to take legal action to recover their losses if a regulated business is in breach of an Ofgem enforcement order. However, there is no right to take action if the business complies with the order. The fact that Ofgem has made an enforcement order does not in itself confer any right to take action. It should also be noted that to date no energy business has breached an Ofgem enforcement order.

10. Depending on the nature of the regulatory breach, consumers may be able to take individual action if, for example, the supplier has breached any contractual obligations. In addition, individual domestic or small business³ consumers may be able to refer their

³ **A small business customer is one with:**

- an annual consumption of electricity of not more than 55,000 kWh, or gas of not more than 200,000 kWh; or
- fewer than ten employees (or their full time equivalent); and an annual turnover or annual balance sheet total not exceeding Euros 2 million.

cases to the Energy Ombudsman if the supplier or distributor is a member of the scheme (but not all energy businesses participate in the scheme). The Ombudsman will deal with individual complaints about energy bills, sales activities, problems arising from switching supplier, or with the supply of gas and electricity. His final decisions are binding on its members and he can award individual compensation of up to £5000. The Ombudsman has no powers to secure collective redress for consumers, although he will inform Ofgem about issues of general concern or potential licence breaches.

11. Consumer Focus can investigate complaints from consumers if they are of wider public interest, but it has no legal powers to secure redress on their behalf. It has, however, successfully negotiated with energy companies to secure redress for consumers, for example, securing payments of £70m for Npower customers in 2010 when the company made changes to its tariff structure without giving adequate notification to its customers.
12. Ofgem has been able to obtain redress for consumers in some cases. Under the legislation, Ofgem can impose a fine which is reasonable to the circumstances of the case and it can take redress into account whether appropriate action has been taken to remedy the contravention or failure when determining the level of the fine. Ofgem has negotiated with companies to secure redress where a breach of a relevant obligation has led to consumer detriment, and licensees have agreed to provide redress on the basis that Ofgem will take this into account when considering a financial penalty (or at an earlier stage when considering whether to open an investigation). Ofgem has negotiated with companies on redress where it considered this would produce a better outcome for consumers than would be the case with the imposition of a financial penalty. However, there have been occasions when Ofgem has been unable to secure appropriate levels of redress.
13. Other regulators have powers to secure redress for consumers. In particular, under the Communications Act 2003, Ofcom can issue a 'notification of contravention' to a communications provider, which may include requiring the provider to remedy the consequences of a breach including for example providing affected consumers with refunds or allowing them to exit contracts without penalty. Where this notification proposes to impose a penalty, this may be both a fixed amount in respect of a past contravention and where the alleged contravention is continuing may be a daily penalty until the contravention is remedied. Any fixed penalty may not exceed 10% of turnover of the provider's relevant business for the relevant period. The level of any daily penalty may not exceed £20k per day. In one case relating to the billing by a telephone company of customers for services that had been cancelled, Ofcom required the company to repay customers and to pay compensation where it was appropriate. As a result, some 62,000 customers received a total of around £2.5m in refunds and good will payments. Ofcom also imposed a fine of over £3m in this case.
14. Currently, whether energy consumers or market participants receive any compensation or other redress depends largely on a company's willingness to provide it or the consumers' readiness to make an application to either the courts or the Energy Ombudsman. Ofgem cannot order a company to rectify any detriment or compensate those who have lost out. The Government proposes to give Ofgem redress powers similar to those of Ofcom. The

Government believes that a power to secure redress would enable Ofgem to better protect the interests of consumers, not least through improving its negotiating position when it is investigating breaches of relevant obligations..

15. In practice, we would expect the proposed powers would generally operate as a backstop for use in those cases where the company in question has failed to address a significant outstanding detriment, and to act as an incentive on companies to offer redress. It is not the Government's intention that the powers should be used as a matter of course to secure redress. Giving Ofgem these powers sends a strong message to the market that companies should themselves be considering ways to compensate consumers disadvantaged by the breach of a relevant obligation as a matter of course. The Government believes that it is good practice for businesses to recognise where they are in the wrong and offer compensation on a unilateral basis where appropriate.

Q. Do you agree that Ofgem should be able to order an energy business that is in breach of its relevant obligations to make appropriate redress to consumers who have suffered a loss as a result of the breach?

16. As stated above, while licence conditions only apply to licence holders, there are some relevant obligations which apply to both licensees and licence exempt undertakings, such as private network operators. It might be argued that including them within the scope of this provision increases the regulatory burden on them. On the other hand, their customers may also suffer financial losses as the result of regulatory breaches and because licence exempt businesses do not participate in the Energy Ombudsman scheme the only current route to redress available to their customers is through the courts.

17. The Government proposes that Ofgem should be able to compel both licensed and licence-exempt undertakings to provide redress where it deems this to be appropriate. In the case of licence exempt undertakings, this change would not impose any new burdens on them as they are already required to comply with the relevant obligations.

Q. Do you agree that Ofgem should be able to compel both licensed and licence-exempt energy undertakings to provide redress when they breach relevant obligations?

18. In respect of Ofgem's new powers, we propose that Ofgem would be able to order redress to be paid not only to domestic consumers of gas and electricity, but also where appropriate to other market participants affected by a breach of relevant obligations, including businesses, generators, networks and suppliers: any entity that has suffered adverse consequences as a result of a breach.

19. The power to obtain redress for other market participants will enable Ofgem to ensure that any unfair advantages gained through misconduct are removed, fostering healthy markets and growth. It is important that those who play by the rules are incentivised to continue to do so rather than witness companies benefitting from rule-breaking. The ability to maintain a level playing field, where those that break the rules cannot benefit

from their wrongdoing at the cost of other market players, promotes fairness and sends a positive message to those entering the market.

20. Ensuring that Ofgem's redress powers extend to other market participants would, in particular, also enable it to help small businesses which suffer harm as a result of a breach of relevant obligations. Like individual consumers, small businesses are vulnerable to wrongdoing, such as misselling, and the impact upon them of any detriment may be significant. Excluding them from the scope of an order for a licensee to make redress would therefore be unfair and unjustified.

Q. Do you agree that Ofgem should be able to order compensation to be paid to other market participants, not just individual consumers?

21. The Communications Act does not specify what kinds of remedy Ofcom can require businesses to implement and this is left to the regulator's discretion. Recent remedies have included refunds and good will payments to consumers. We propose that Ofgem should have similar discretion to specify what kind of remedy is appropriate to the circumstances of the case. In some cases, direct "pound for pound" refunds will be appropriate but in other cases it might be impossible or disproportionate for businesses to have to identify individual customers who have been affected by a regulatory breach – in these cases, good will payments or public apologies may be appropriate.

Q. Do you agree that Ofgem should have discretion to decide what form of redress is appropriate to address the detriment caused by regulatory breaches?

22. Where Ofgem does need to use the proposed powers, it would not be just to cap a company's liability for its wrongdoing: the wrong should be rectified whatever the cost. Moreover, capping liability allows a company to carry out a 'risk evaluation' to assess where committing a breach might be financially advantageous and undermines the deterrent effect of the power to order licensees to make redress. Ofcom's powers to secure redress are not subject to a cap and we do not intend to cap Ofgem's redress powers.
23. We do not propose any changes to Ofgem's fining powers. Fines and redress serve different purposes. A fine is punitive whereas redress seeks to address the harm caused to those affected by the breach and we see no justification for reducing the existing cap on financial penalties of 10% of the company's annual turnover. There will be occasions where redress is ordered as an alternative to the imposition of a fine, and there will sometimes be wrongdoing that does not affect consumers or other market participants directly so it does not necessitate the making of an order for redress. Where appropriate Ofgem would be able to fine a company alongside making an order for redress.
24. In cases where an order for redress is made alongside the imposition of a fine, we would expect Ofgem to continue to take this redress into account in setting the level of the fine and on occasions to reduce the level of fine, although depending on the nature of the breach of a relevant obligation, it may still be appropriate for Ofgem to impose a substantial fine. As is the case now, it would be for Ofgem to determine what fine is reasonable in the circumstances of an individual case.

25. The Government is proposing that where Ofgem is satisfied that a breach of a relevant obligation has taken place it will be able to make an order to require the company in question to remedy the consequences of the breach, so that consumers and other market participants do not lose out. Ofgem gathers evidence of detriment in the course of its investigation of alleged breaches in order to decide on the appropriate level of penalty. This evidence can be used to inform its thinking on the scope and level of any redress to be made, without adding to the length of the investigation or significantly increasing the burden on companies under investigation to provide information.
26. Obviously, it is not possible to predict the likely substance of orders for redress. This will depend on the nature of the detriment which has resulted from the breach at issue in a particular case. Each case will require consideration on its own facts. Determining the appropriate redress is likely to require some discussion with the company and those that have suffered detriment.
27. In the case of Ofgem, we anticipate that Orders for redress may include provisions on “pound for pound” compensation for consumers who suffer a measurable loss, good will payments where it is difficult or impractical to determine the individual loss and requirements relating to information and publicity.
28. We are proposing that the procedures for requiring redress should be modelled on the current provisions for imposing financial penalties in the Gas Act 1986 and the Electricity Acts 1989. Ofgem will be required to give notice to the company and any other affected party at least 21 days before making the order for redress. At this point Ofgem will be required to set out which condition has been breached, how in its view the licensee has breached it and the remedy it deems appropriate. The licence holder will have a minimum of 21 days to make representations to Ofgem regarding the proposed order for redress.
29. If Ofgem, after considering representations from the licensee, decides to vary the order for redress, it will need to set out in the order the proposed variations and the reasons for it, and then allow a further 21 days for representations. In the event that the licence holder still contests the order, we envisage the current statutory right of appeal on a penalty to the court would also apply to orders for redress. Under the Gas Act 1986 and Electricity Act 1989, energy businesses currently have a right of appeal to the courts if they are unhappy about being fined, the amount of the fine or the time they have been given to pay it. We intend that similar rights of appeal would apply in respect of redress orders.
30. As with financial penalties, we propose that there should be a time period of up to 5 years from the date of the breach of relevant obligation for the making of an order for consumer redress.
31. It is envisaged that the Authority will issue a statement of policy on the use of the proposed powers. This would be separate from Ofgem’s financial penalties statement but may necessitate consequential changes to be made to that statement.
32. We have prepared an Impact Assessment (insert link) for this proposal but, as stated above, it is difficult to assess what the likely impact of this change may be as we cannot predict how much compensation consumers may receive or the costs businesses may

face (although it is probably reasonable to assume that both of these will increase). We welcome any comments from consultees that would help in our assessment, in particular from businesses on the range of costs they anticipate they might be faced with if they have to refund a substantial number of their customers or any other information that would assist us in estimating the impact of the new power.

Q. Can energy businesses provide us with any information about administration or other costs they anticipate they might face should Ofgem require them to provide redress to consumers?

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