

**Decision of the Gas and Electricity Markets Authority, following an investigation into compliance by British Gas Trading Limited with its obligations under standard licence condition 20 of its electricity supply licence.**

**18 June 2003**

1. This document constitutes a notice, published in accordance with section 27A (5) of the Electricity Act 1989 stating that the Gas and Electricity Markets Authority (the Authority) is satisfied that British Gas Trading Limited has contravened Standard Licence Condition 20 of its electricity supply licence and that in consideration of that contravention it confirms the decision to impose a financial penalty of £150,000 on British Gas Trading Limited.
2. The Authority has a principal objective to exercise its functions to protect the interests of gas and electricity consumers. The Authority also has general duties which apply to the performance of its functions, including a duty to have regard to the interests of:
  - (a) individuals who are disabled or who are chronically sick;
  - (b) individuals of pensionable age;
  - (c) individuals with low incomes; and
  - (d) individuals living in rural areas.
3. The Authority grants licences for the supply of electricity. It has a duty to keep under review activities in the areas to which electricity licences apply. It also has a duty to take enforcement action where it is satisfied that a licence obligation is being, or is likely to be, contravened and may impose a financial penalty in respect of a past or continuing contravention.
4. Ofgem has investigated British Gas Trading Limited's compliance with standard licence condition 20 of its electricity supply licence. At its meeting on 15 April 2003,

the Authority, after consideration of oral representations made by British Gas Trading Limited, concluded that British Gas Trading Limited had contravened standard licence condition 20 of its electricity supply licence.

- 5 Section 27A (1) of the Electricity Act 1989 states that where the Authority is satisfied that a licence holder has contravened or is continuing to contravene any relevant condition or requirement, the Authority may impose on the licence holder a penalty of such amount as is reasonable in all the circumstances of the case.
- 6 Under section 27A (8) of the Electricity Act 1989 no penalty imposed by the Authority under this section may exceed 10% of the turnover of the licence holder as ascertained in accordance with The Electricity and Gas (Determination of Turnover for Penalties) Order 2002 (SI 2002/1111). The turnover of British Gas Trading Ltd for the financial year ending 31 December 2001 was £7,391,657,000.
- 7 On 16 April 2003, in accordance with section 27A (3) of the Gas Act 1986 the Authority gave notice that it proposed to impose a penalty of £150,000 on British Gas Trading Limited.

#### **A Background**

- 8 British Gas Trading Ltd is a wholly owned subsidiary of Centrica plc.
- 9 Ofgem has conducted an investigation into British Gas Trading Ltd's compliance with Standard Licence Condition 20 of its electricity supply licence, specifically whether British Gas Trading Ltd had complied with the requirements of the relevant paragraphs of the Master Registration Agreement, the MRA.

#### **B Information provided to Ofgem**

- 10 On 1 May 2002 Ofgem received a complaint alleging that British Gas Trading Ltd had objected incorrectly to the transfer of a direct debit electricity customer on the grounds of outstanding debt.

11 Specifically the complainant alleged that, before making the objection, British Gas Trading Ltd had failed :

- To make a written demand for the outstanding sum; and
- To allow the customer 28 days in which to make payment before making the objection.

12 Ofgem analysed statistics relating to electricity transfer requests and objections submitted by all suppliers, including British Gas Trading Ltd, and as a result decided to investigate British Gas Trading Ltd's compliance position.

### **C Findings**

13 The Authority is satisfied that between 1 January 2002 and 31 July 2002, British Gas Trading Ltd contravened Standard Licence Condition 20 of its electricity supply licence for the following reasons.

14 A procedural instruction current between 1 January 2002 and 4 August 2002 as to when British Gas Trading Ltd staff should object to a transfer was incomplete. It did not reflect the fact that the annual settlement statements issued to British Gas Trading Ltd's direct debit customers do not contain a demand for any arrears outstanding and are worded "This is for information only". The requirement set out in paragraph 16.1.2 of the MRA cannot be satisfied by the issue of such a statement.

15 British Gas Trading Ltd failed to identify this problem through its own supervisory processes, and did not amend the instructions until 5 August 2002, after Ofgem had raised this matter.

16 British Gas Trading Ltd has accepted the estimate of 2,900 customers that were prevented at some time during the relevant period from transferring to another supplier.

## **D Enforcement**

- 17 If the Authority is satisfied that a licence holder is contravening, or is likely to contravene any relevant condition or requirement, section 25 (1) of the Electricity Act 1989 requires the Authority, subject to subsections (2), (5) and (5A) of section 25 and section 25 of the Electricity Act 1989, by final order, to make such provision as is requisite for the purpose of securing compliance with that condition or requirement.
- 18 Section 25 (2) of the Electricity Act 1989 states that, subject to subsections (5) and (5A) of section 25 of the Electricity Act 1989 , where it appears to the Authority that a licence holder is contravening or is likely to contravene any relevant condition or requirement and that it is requisite that a provisional order be made the Authority shall (instead of taking steps towards the making of a final order) by a provisional order make such provisions as appears to the Authority requisite for the purpose of securing compliance with that condition or requirement.
- 19 Section 25 (5A) of the Electricity Act 1989 states that the Authority is not required to make a final order or make or confirm a provisional order if it is satisfied:
- a) that the licence holder has agreed to take and is taking all such steps as it appears to the Authority for the time being to be appropriate for the licence holder to take for the purpose of securing or facilitating compliance with the condition or requirement in question; or
  - b) that the contraventions were or the apprehended contraventions are of a trivial nature.
- 20 In correspondence and meetings with the Authority British Gas Trading Ltd has confirmed that it has taken steps that it believes will secure compliance with Standard Licence Condition 20. It is now checking all transfer requests.

21 In the light of these actions the Authority is unable to make a final order or make or confirm a provisional order as it is not satisfied that British Gas Trading Ltd is contravening, or is likely to contravene, Standard Licence Condition of 20 of its electricity supply licence. The Authority will continue to monitor British Gas Trading Ltd's compliance with Standard Licence Condition 20.

## **E Financial Penalties**

22 Section 27A (1) of the Electricity Act 1989 states that, where the Authority is satisfied that a licence holder has contravened or is contravening any relevant condition or requirement, the Authority may impose on the licence holder a penalty of such amount as is reasonable in all the circumstances of the case.

23 Section 27A (2) of the Electricity Act 1989 states that the Authority shall not impose a penalty on a licence holder where it is satisfied that the most appropriate way of proceeding is under the Competition Act 1998. The Authority considers that this matter is clearly an issue of licence compliance which may be dealt with most appropriately as such. The Authority is not satisfied that the most appropriate way of dealing with it would be under the Competition Act.

24 In accordance with section 27B of the Electricity Act 1989 the Authority has prepared and published in April 2001 a statement of policy with respect to the imposition of penalties and the determination of the amount.

25 Section 27A (3) of the Electricity Act 1989 requires the Authority before imposing a penalty on a licence holder to give notice:

- a) stating that it proposes to impose a penalty and the amount of the penalty proposed to be imposed;
- b) setting out the relevant condition or requirement or the standard of performance in question;

- c) specifying the acts or omissions which, in the opinion of the Authority, constitute the contravention or failure in question and the other facts which, in the opinion of the Authority, justify the imposition of a penalty and the amount of the penalty proposed; and
- d) specifying the period (not being less than 21 days from the date of publication of the notice) within which representations or objections with respect to the proposed penalty may be made.

26 In deciding whether or not to impose a financial penalty, the Authority considered:

i. Factors tending to make the imposition of a penalty more likely:

- The contravention has damaged the interests of consumers or other market participants.

*An erroneous objection may be financially disadvantageous and is likely to be inconvenient for consumers. Customers of a supplier have a right to expect that switching supplier should be a straightforward process with little inconvenience.*

*When that is not the case their perceptions of the competitive market may be damaged. Competitors will have incurred costs through their sales and marketing activity and their attempts to process transfers which subsequently failed.*

*Competitors will have lost the margin that they would otherwise have gained.*

- To do so would be likely to create an incentive to compliance and deter further breaches.

*The imposition of a financial penalty would send a firm signal to the licence holder and other licence holders that the Authority will not allow suppliers to avoid their responsibility for ensuring that the facility to object is not used to retain customers outside of the permitted circumstances.*

ii. Factors tending to make the imposition of a financial penalty less likely:

- If the contravention were of a trivial nature.

*British Gas Trading Ltd has accepted that the contravention was not of a trivial nature and the Authority agrees.*

- That the principal objectives and duties of the Authority preclude the imposition of a penalty.

*The principal objectives and duties of the Authority do not preclude the imposition of a penalty in this case. The Authority sees no reason to believe that a penalty would be against consumers' interests or would hinder competition.*

- That the possibility of a breach would not have been apparent to a diligent licence holder.

*The Authority considers that a diligent licence holder would have established procedures for ensuring compliance with its licence obligations. After Ofgem raised this matter with British Gas Trading Ltd, the company carried out its own compliance audit and instituted quality checks on all objections.*

Taking these factors into consideration, the Authority considers that the imposition of a penalty is appropriate in this case.

27 In its initial calculation of the level of a financial penalty the Authority considered the following factors:

- Seriousness of the breach

*The facility to object to a customer transfer, within the gas and electricity supply markets, is an uncommon feature in markets generally. It provides protection to suppliers in prescribed circumstances and restricts the free movement of consumers between suppliers. The ability to switch is at the heart of competition.*

*It is essential that the facility is used appropriately, to ensure that consumers are not disadvantaged. The Authority considers that erroneous objections interfere with the effective working of the electricity supply market, that they have the potential to damage customers' willingness to engage with the market and have an adverse impact on the way in which the market and the benefits of competition are perceived by consumers. However, this breach should be considered in the context of the full range of possible licence breaches. There has been no threat to safety, and no competitors have been driven from the market. In determining the seriousness of the breach the Authority took account of the extent of the breach, the number of customers affected and that it is not likely to have caused widespread damage to consumer confidence.*

- Degree of harm or increased cost incurred by consumers or other market players  
*The Authority considers that erroneous objections may be financially disadvantageous and inconvenient to consumers. British Gas Trading Ltd declined to compensate these consumers. Competitors have incurred costs that are probably unrecoverable in practice, through wasted sales activity and attempts to process transfers which subsequently failed. They also lost the margin that they might otherwise have gained.*
- Duration of the licence breach  
*The evidence presented as a result of this investigation covers the period from 1 January 2002 to 31 July 2002. Secondary legislation essential to the financial penalty process came into force on 12 April 2002. The Authority therefore in this matter cannot impose a financial penalty for a breach before that date, nor for a breach which took place more than one year before the date of service of this notice.*



- Any gain (financial or other) by British Gas Trading Ltd.

*The Authority has considered potential benefits to British Gas Trading Ltd from objecting incorrectly, ie. from customers prevented from transferring and the potential value of those customers. Some customers will have since successfully transferred.*

28 In its published guidance the Authority stated that it would look at factors that could lead to an increase in the level of the penalty. These include, but are not limited to:

- Repeated contravention or failure

*Each incorrect objection was a failure to comply with the MRA and thus, Standard Licence Condition 20. The failures identified by the Authority were repeated over the relevant period, and had continued through the period of investigation, though when British Gas Trading Ltd became aware of the issue it took rapid action to prevent recurrence.*

- Continuation of contravention or failure after becoming aware of the contravention or failure, or becoming aware of the start of Ofgem's investigation  
*Once the company became aware of the investigation, it moved quickly to assess its own compliance and change its processes.*

- Involvement of senior management in any contravention or failure

*It appears that senior management failed to control the way in which objections policy was applied in a specific set of circumstances, rather than designing it with the intention of wrongly retaining customers.*

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

*The facility to object is not new to the market, and there can be no doubt that British Gas Trading Ltd will have been aware of its obligations – which have been the subject of a number of industry and Ofgem meetings.*

- The extent of any attempt to conceal the contravention or failure from Ofgem  
*British Gas Trading Ltd co-operated with the investigation.*

29 Under the Authority's published guidance it will consider a number of factors that could tend to decrease the level of any penalty. These factors may include, but are not limited to;

- the extent to which the licence holder has been taking steps to secure compliance, either specifically or by maintaining an appropriate compliance policy, with suitable management supervision  
*British Gas Trading Ltd's policy was appropriate but it was not properly implemented in respect of the particular situation where a customer moves house.*
- Appropriate action by the licence holder to remedy the contravention or failure  
*The Authority has noted that, from 5 August 2002, British Gas Trading Ltd has had in place revised procedures which it believes will secure compliance with the relevant licence condition.*
- Evidence that the contravention or failure was generally accidental or inadvertent  
*British Gas Trading Ltd is responsible for ensuring its procedures are adequate to secure compliance. The breach may have been inadvertent, but British Gas Trading Ltd did not have in place at the time effective procedures for detecting such errors.*
- Reporting the failure to Ofgem  
*This did not happen before the start of the investigation.*

- Co-operation with Ofgem investigations

*British Gas Trading Ltd has co-operated with the investigation.*

30 At its meeting on 16 April the Authority proposed to impose a penalty of £150,000 and invited representations from interested parties, on its proposal.

## **F Representations**

31 The Authority has considered the four written representations it received, two of which were confidential and one which contained a confidential extract.

32 energywatch warmly welcomed the investigation, was satisfied with the outcome, but stated that it believed that consumers badly affected by any licence breach should be compensated.

33 British Gas Trading Limited accepted that it had breached the requirements of the licence condition and accepted the proposed penalty.

## **G Decision**

34 After considering all of the responses, the Authority must confirm, vary or withdraw the proposed penalty.

35 If the Authority decides to confirm the proposed penalty it is required by section 27A (5) of the Electricity Act 1989 to issue a notice:

- (a) stating the imposition of the penalty and its amount;
- (b) setting out the relevant condition or requirement or the standard of performance in question;
- (c) specifying the acts or omissions which, in the opinion of the Authority, constitutes the contravention or failure in question and the other facts which, in the opinion of the Authority, justify the imposition of the penalty and the amount; and
- (d) specifying a date, no earlier than the end of 42 days from the date of service of the notice on the licence holder, by which the penalty is required to be paid.

- 36 For the purpose of paragraph 35 (a) and after considering all the representations received, the Authority hereby confirms the decision of 16 April 2003 to impose a penalty of £150,000 on British Gas Trading Limited.
- 37 For the purpose of paragraph 35(b) the relevant licence condition or requirement, or the standard of performance in question, is standard licence condition 20 of British Gas Trading Limited's electricity supply licence.
- 38 For the purpose of paragraph 35 (c) the acts or omissions which, in the opinion of the Authority constitute the contravention or failure in question and the other facts, which in the opinion of the Authority, justify the imposition of a penalty and the amount of that penalty are set out in sections C,D and E of this notice.
- 39 For the purpose of paragraph 35 (d) the penalty must be paid to the Authority no later than 31 July 2003.
- 40 In accordance with section 27A (6) of the Electricity Act 1989 British Gas Trading Limited may, within 21 days of the date of service of this notice, make an application to the Authority for it to specify different dates by which different portions of the penalty are to be paid.
- 41 If the whole or any part of the penalty is not paid by the date it is required to be paid, then in accordance with section 27D (1) of the Electricity Act 1989, the unpaid balance from time to time shall carry interest at the rate for the time being specified in section 17 of the Judgements Act 1838.
- 42 In accordance with section 27F of the Electricity Act 1989, where a penalty imposed, or any portion of it, has not been paid by the date on which it is required to be paid, the Authority may recover from British Gas Trading Limited, as a civil debt due to it, any of the penalty or interest which has not been paid.

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For and on behalf of the Gas and Electricity Markets Authority