Response to Consultation on Approach to Enforcement

Consultation on revising [the UR] enforcement procedure and financial penalties policy

On behalf of

AES Kilroot Power Ltd and AES Ballylumford Ltd

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Prepared by AES Commercial Department,

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1: Introduction

AES Kilroot Power Limited and AES Ballylumford Limited (together "AES" in this document) welcome the opportunity to comment on this consultation from the Utility Regulator ("UR") in relation to their "Approach to Enforcement" (the "Consultation"). Although they are separate licensed entities, AES Kilroot Power Ltd and AES Ballylumford Ltd are submitting a combined response to this Consultation expressing their shared views..

It should be noted that AES has outlined the ten (10) Key Comments it wishes to make in Section 2 of this consultation response.

While Section 3 contains more detailed comments, they should also be given due regard when reviewing this consultation response overall.

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2: Key Comments

1) Although the Consultation appears to be undated, we note that it was published on 28 February 2018 seeking responses by 9 April, a period of under 6 weeks, with the Easter holiday period intervening. We further note that the email from UR to market participants advising them of this new Consultation paper issued over a week (7th March) after the Consultation is reported to have gone live, and further that the letter sent out by UR to market participants to highlight the Consultation was dated 20th March (AES received same on 22nd March) some 3 weeks after the Consultation is reported to have been published.
    - Given the nature of the issues being consulted upon, and the importance of those both for licensees and consumers in Northern Ireland, we believe that a period which is effectively 5 weeks (at best) is very brief and appears to be far from the tenor of the Better Regulation principles, which require consultation to be 'effective' and proportionate. Such a period does not appear to be effective or proportionate, and is not in the interests of consumers. AES has requested an extension to the consultation period.
2) In addition, an adoption of the revised documents in May 2018, as envisaged in the Consultation paper (para 14), also appears to be contrary to the Better Regulation principles, which require a sensible period before any such revisions take effect, once the consultation has concluded and once a regulator has devoted sufficient time to assessing responses and coming to a decision applying its objective and duties. We believe that a period which could, at most, be 7 weeks and 3 days (but which could be as little as 3 weeks) to be wholly inadequate, and not in accordance with the objective and duties of the UR.

3) We also have a concern that the Consultation on its face suggests that the UR may have already come to a conclusion on points which the paper states are being consulted upon. This is contrary to the general principle of fair consultation, where consultation should be at the 'formative stages' of thinking to allow meaningful consultation. This admission that some issues have already been decided cuts directly across these requirements. Some examples of this include the following paragraphs, which explicitly reflect that minds appear to have already been made up, and which leads one to question the nature and value of this consultation process:
    - In para 16 of the Consultation it states "*we concluded that the overall aim of [the] Enforcement Procedure should be expanded*", suggesting that a conclusion was reached before the consultation.
    - In para 18 the Consultation states "*we concluded that our approach to enforcement should be expanded to provide for…Prioritisation principles to guide us in deciding when to take enforcement action…..Settlement of cases….Publication of information on investigations and case outcomes*".

    Further in para 14 of the Consultation it clearly states that "*Following consideration of the responses to this consultation we will publish the revised versions of the enforcement procedure and financial penalties policy. We expect this to be no later than May 2018*". Firstly, it appears to be at odds to other consultation processes to have an intended decision date referred to in a consultation document. Secondly, we have already made the point that this period appears too short, but additionally the paragraph indicates that whatever the responses to the consultation, and therefore whatever changes may be required to be made to the proposed documents being consulted upon assuming a valid consultation exercise, no further consultation is intended. If the consultation exercise produces changes that differ from those consulted on, it is incumbent on the UR that it should undertake a further consultation to ensure that stakeholders have an opportunity to see what different changes are being proposed, and this is proposed to be in line with best practice.

4) The UR makes a point in para 17 of the Consultation that it has reviewed the enforcement policies and procedures of other economic regulators to inform its approach. This is indeed a positive step. However, in light of this it is surprising, and disappointing, that in the draft policies and procedures accompanying the Consultation there is seemingly no reference to the UR's duty to have regard to the need to secure that licence holders are able to finance their relevant activities or consideration of the impact of any financial penalty on the financial viability of licensees, which also goes to the heart of the principal objective to protect the interests of consumers. We refer to Ofgem in its Financial Penalties Policy (para 5.29) where it provides that it will "*consider the effect of a proposed penalty……on the financial viability of a regulated person and may make adjustments accordingly in light of its*

principal objective". We believe it is reasonable that the UR should include a similar concept in it's equivalent NI document, which would appear to be required in order to reflect both best practice and their relevant obligations.

- Further we note a greater level of detail in the equivalent Ofgem document, giving greater clarity to deal effectively with these complex issues, and believe the UR proposed document would benefit from similar greater detail. It is hoped that the UR intends to allow their proposed document to benefit from further development as part of this consultation.

5) The Consultation and the proposed enforcement policy document sets out proposals in relation to publishing information about investigations and any decisions. Currently the limited requirements for prior notice to licenced entities and that even such limited notice is for "information only", are considered insufficient to reflect a true solution-orientated process of engagement. This is a clear link between what might be published under the Enforcement Procedure and the requirements of Article 63 of The Energy (Northern Ireland) Order 2003 which restricts the disclosure of information obtained by the UR unless certain exceptions apply. The policy document being consulted upon here should reflect these restrictions as they apply to the UR, and in general. Further as outlined in comments on para 42 of the Consultation below where an Alternative Resolution has been agreed any published information (i) should not name the entity (ii) should not allow any professional third party to deduce who the investigation or case related to (iii) should not contain any information that could be deemed as commercially sensitive or secret to the entity involved in the investigation or case.
6) The Alternative Resolution process should be considered in all investigations and cases, and must remain a mechanism available to resolve any issue throughout the full process of an investigation or case, including after the Summary of Initial Findings has been issued.
7) The "Investigation Team", the "Settlement Committee" and the "Enforcement Committee" should all act independently and be unbiased, to ensure a fair and reasonable outcome to the process, having full regard to both parties' views and all pertinent facts. To achieve this goal, there should be a number of independent members appointed to these groups who are truly independent of the UR and market participants.
8) Throughout the Enforcement Procedure and Financial Penalties Policy due regard should be taken of the UR's Obligations to Licenced Entities, and the reasonable right and expectations of such entities to make a reasonable return and be able to finance their activities
9) In relation to how the UR acts as part of the enforcement process the regulator should have an overarching obligation in the first instance to:
    - engage with regulated entities, to outline any concerns they may have in terms of a potential or actual contravention of any legislative or licence obligation, and

- understand the reasons for the potential or actual contravention, and to assess whether the party acted in a reasonable manner given all its duties and responsibilities under its licence and otherwise; and
- work with such regulated entity to try to find a reasonable solution to the potential or actual issue, ensuring to act reasonably at all times, and to provide sufficient and reasonable time for any such resolution to be given effect

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3: Detailed Comments

Section 1:

- **Section 1 Bullet 2** – The UR amended the "Financial Penalties Policy" in 2016. The UR has not advised why less than a year later they included a further review of this in their 2017/18 work programme. The UR are requested to advise as to the reasons for a further amendment so soon after the last review which came into effect on 11th march 2016.

Section 2

- **Section 2 – Clause 15** – UR have outlined one of the reasons for reviewing and amending the Enforcement Procedure was to ensure it "is aligned with best practice". No details have been provided as to how the proposals outlined in this consultation document align with best practice. How did the UR access this criterion?
  The review of the Enforcement Procedure appears to have looked at how multiple regulators approach this activity, and as a result of this review the UR has determined that 4 changes were required to facilitate (i) Prioritisation principles (ii) Alternative Resolutions regimes (iii) Settlement of Cases and (iv) Publication of investigations and outcomes.
  However, the review of the Financial Penalties Policy has focused solely of the Ofgem regime, with little detail as to why this was the preferred regime, and no detail as to why other regulatory regimes were not considered. The UR are asked to comment on this.
- **Section 2 – Clause 20** – UR have outlined their view to give "more prominence" to the "concept" of (i) the gain of the company and (ii) the detriment to the customer, arising from a contravention. No reasons have been given for this, and no examples have been provided as to where this has been implemented in other jurisdictions, and how it has worked/not worked.

Section 3: Proposed Changes to UR's Enforcement Approach

- **Clause 23** – AES does not agree that an aim of the Enforcement Procedure is to "*ensure that regulated companies comply with their legislative and licence obligations*". We contend that the aim should be as outlined in Clause 24 that the aim of any Regulator is to "incentivise compliance". Incentivising compliance (as opposed to "ensuring compliance") is a sufficient mechanism, and akin to what is used in many jurisdictions, given the need for regulated entities to comply with the full suite of their legislative and licence obligations.
- **Clause 26**: It is not apparent how publishing information on investigations and case outcomes will "*ensure accountability and consistency*" in UR's decision making. The UR is requested to provide an explanation of how this is the case and why it would not be the case otherwise.
- **Clause 33** – The UR has set out in para 33 some potential Enforcement Prioritisation Principles
    - **Bullet Point 7:** Given the extremely serious potential impacts of any investigation and or case for a licensed entity, we believe that any investigation and or case should be carried out by either an independent, professional, and experienced third party, or by agroup which has independent third party knowledgeable members appointed to it. This third party should be selected by a steering group made up of representatives from both the regulator and industry. Such steering group should also assess the performance of such appointed third party entity on an annual basis.
      An independent third party professional entity is necessary due to (i) the seriousness of the enforcement scenarios (ii) the fact that there will always be different views on particular aspects of all cases, and that (iii) there will often be relevant background information, and rationale for actions, that will need to be considered.
    - Principles not mentioned in the Consultation that AES request are added include the following:
        - The UR should have an overarching obligation in the first instance to;
            - engage with regulated entities, to outline any concerns they may have in terms of a potential or actual contravention of any legislative or licence obligation, and
            - try to understand the reasons for the potential or actual contravention, and to assess whether the party act in a reasonable manner given all its duties and responsibilities
            - work with such regulated entity to try to find a reasonable solution to the issue, ensuring to provide sufficient and reasonable time for any such resolution to be given effect
        - 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

- **Clause 36** – AES does not believe that there should be any restriction in the potential use of the Alternative Resolution process. As currently drafted this clause appears to suggest that the UR will apply the prioritisation principles to determine "*if a case is suitable for alternative resolution*". AES believes this is unnecessarily restrictive, as the key is to get a desirable resolution and outcome, and an alternative resolution may be the best route in many if not all potential situations.
- **Clause 39** – AES does not support the proposal that no further Alternative Resolution proposals will be considered by UR once the Summary of Initial Findings have been served on the Company. This AES contends is overly and unnecessarily restrictive. Any and all proposals must remain open for consideration at all times during the process, as there is frequently potentially many ways to reach a desirable outcome, and many may not have been considered in the early stages of the process.
- **Clause 42**: Where a case has been closed by means of an Alternative Resolution process, the licenced entity should be allowed to retain their anonymity and thus not be named in any report issued by the Regulator. Naming such entities could have damaging impacts on their reputation, and by reaching agreement with the UR via an Alternative Resolution it is clear that such party has made appropriate amends so it appears reasonable and logical to argue there is nothing of material benefit to be gained by naming the entity. If, however, the Regulator wishes to advertise details of the investigation activity it is involved in, this is reasonable, as long as any details so published where an Alternative Resolution has been agreed (i) will not allow any professional third party to deduce who the investigation or case related to (ii) does not contain any information that could be deemed as commercially sensitive or secret to the entity involved in the investigation/case.
- **Clause 46:** Once a desirable outcome is achieved, it appears unnecessarily onerous to insist that a party must "*admit to **all** the contraventions that are under investigation*" as it may be the case some are more important than others. The UR are asked to reconsider this restriction, and allow a degree of reasonableness to be applied here.
- **Clause 47:** Settlement should not be restricted "*only in cases where a financial penalty is in prospect*". This appears overly restrictive and may prevent workable reasonable resolution to issues from being achieved to the mutual agreement of all parties.
- **Clause 48:** It should not be the case that the degree of discount is solely related to how early a settlement agreement is signed. There can be many other factors which with the appropriate flexibility on how the discount can be applied could have yielded a more desirable outcome for UR.

- **Clause 52:** As drafted this is highly confusing and appears to suggest that there may be occasions where discounts will not apply even when settlement has been reached. The UR are asked to clarify.

Annex 1: Enforcement Policy Approach and Procedure

- **Clause 1.6:** We query the wording proposed in para 1.6 of the proposed enforcement policy document. This states that "*Our procedure does not apply in respect of any enforcement decision in relation to the all-Ireland Single Electricity Market*".
  Firstly, we suggest that what was meant to be written here was the "all-Island" SEM, and ask UR to confirm that there was an error here.
  Secondly, the enforcement policy document seems to exclude many elements of enforcement, as most enforcement issues related to the electricity market will very likely relate to the all-Island market. However this is in contract to Annex 3 Clause 1.6 where UR suggest they "*will make any decision in relation to the imposition of a penalty …..to …. electricity (including the single wholesale market for electricity)*". UR are asked to clarify the situation here.
- **Clause 2.2:** The approach to (i) investigating any potential contraventions and (ii) making enforcement related decisions should include the design facet/criteria of having to be "reasonable" in all circumstances.
- **Clause 2.7, 2.8, 2.9:** The process as outlined fails to recognise the importance to companies of not wishing to have details of any "potential" contravention published broadly prematurely and unnecessarily. It is suggested that nothing should be published until a final decision has been made, and even then, anything published should be sensitive to the particular circumstances of the case and the company involved. The entity should not be named if an Alternative Resolution is achieved, and more limited details should be provided in this case also. Providing details of cases on a regular basis as "News" items on the UR Website seems inappropriate given the seriousness of the situations likely to be involved.
- **Clause 2.10, 2.11 and 2.12** – It must be recognised that the concerns raised in the previous Bullet point will act as a deterrent for companies to act as is desirable for the UR outlined in Clause 2.10 and 2.11.
- **Clause 3.10** – In many sections of the paper UR outline their aim to protect the interests of consumers, yet in this clause UR also refer to protecting the interests of "the market". UR are asked to clarify their legislative and other obligations to protect the market.
- **Clause 3.14** – Please refer to comments on Clause 39 and 44 above.
- **Clause 3.17** – Please refer to Comments on Clause 42, and to clauses 2.7, 2.8 and 2.9 above. No company should be named when an Alternative Resolution has been agreed, and only certain information should be published in such cases.

- **Clause 3.20** – It is not clear why there is a requirement for a "*public consultation on the amount of any potential penalty*". If the process were to go to conclusion, UR would decide the potential fine. The benefit of Settlement is to reach agreement sooner, and to allow a discount of the potential UR decided fine to occur. As such it does not appear appropriate to hold a public consultation.
- **Clause 3.26** – It is encouraging that UR wish to have the "enforcement committee" independent and unbiased. However to truly ensure this the committee must include a number independent representatives . No detail has been provided as to the make-up of the representation of the Enforcement Committee) or the Investigation Team who also should act independently and in an unbiased manner, and thus should also contain independent members). The UR are asked to provide this detail to give market participants the comfort that this committee (and team) will contain independent members.
- **Clause 3.27** – Caution is stressed in the event that UR receives a complaint from a third party about a potential contravention of a licenced entity, as there may be competitive or personal interests at play which needs to be fully investigated in advance of any communication with the Licenced Company especially given the seriousness of this process, and the potential material negative impacts on licenced companies related to the publication of investigation/case information as outlined in this consultation.
- **Clause 3.33** - Please refer to comments on Clause 3.17. No company should be named when an Alternative Resolution has been agreed, and only certain information should be published in such cases.
- **Clause 3.36** – It is suggested to be inappropriate to name a company where a case has been opened but the outcome is unclear. Natural justice would suggest parties should be considered innocent until proven guilty, and as such naming entities broadly to the market at this early stage appears unwise and inappropriate, given the potential negative public perception of such entities in such a case, even if it is found at a later time that there is no case to answer. It is suggested that no naming of companies should occur until a Summary of Initial Findings (SIF) has been issued.
- **Clause 3.42** - Please refer to comments on Clause 3.17 and 3.33. No company should be named when an Alternative Resolution has been agreed, and only certain information should be published in such cases
- **Clause 3.44** – This outlines a requirement for the regulated entity to respond within 21 days. Firstly, it seems more appropriate to set this to 28 days similar to the timing outlined in Clause 3.54. Secondly, even with this timing, given the potential complexity of some potential issues, it is suggested that UR allow some flexibility to themselves and the regulated entity in relation to this timeline, as some information may take a considerable time to gather, especially if third party or experts are required to be involved.
- **Clause 3.6:** As outlined in Key Comment (4) in Section 2 above, In considering the financial penalty to apply, UR should take into account the potential impact of the penalty on the viability of the entity to which it is

intended to be applied. We refer to Ofgem in its Financial Penalties Policy (para 5.29) where it provides that it will "*consider the effect of a proposed penalty……on the financial viability of a regulated person and may make adjustments accordingly in light of its principal objective*". We believe it is reasonable that UR should include a similar concept in their equivalent NI document.

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