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Your Reference 0115/0115A

Re: Modification Proposal 0115/0115A: 'Correct Apportionment of NDM Error'

Dear Julian,

Thank you for your invitation seeking representations with respect to the above Modification Proposals.

National Grid Distribution is able to offer support in principle for implementation of Modification Proposal 0115 although this is heavily qualified in a number of respects. The extent of this qualification is such that we believe it may be that some elements of Proposal 0115 do not better facilitate the relevant objectives under Standard Special Condition A11.1(d) of the Transporters Licence.

We oppose implementation of alternative Modification Proposal 0115A.

We have participated in all discussions pertaining to these Proposals within the UNC Distribution Workstream and in addition have sought information from our service provider, xoserve to substantiate our views. It is likely that some of the information identified within this representation will appear in responses from other Distribution Network Operators (DNOs).

Modification Proposal 0115 proposes that all Reconciliation by Difference (RbD) energy be smeared across all Non Daily Metered (NDM) Supply Points. The current RbD process smears primary reconciliation only to Smaller Supply Points (SSP).

Modification Proposal 0115A advocates a similar regime except that any Monthly Read Meter would be excluded from the Larger Supply Point (LSP) smear.

The original RbD concept was that as energy within an LDZ was whole and known, any over or under allocation to the LSP market would generate an equal and opposite movement within the SSP market. In practice this principle is only 100% valid if all gas offtake is accounted for and all energy is billed correctly. Where there are unknown energy losses, such as through undiscovered theft or unregistered Supply Points, the NDM allocation process forces energy wholeness by over allocating to all known Supply Points. The LSP known Supply Points will then reconcile correctly, leaving all energy arising from any issues to be borne by the SSP market.

RbD charges are typically a debit to SSP Users. Both Modification Proposals challenge whether it is equitable for SSP Users to pay for the unknown energy losses when these may occur within the LSP market.

In general, there are a number of areas where the Proposers have a justifiable argument. For example, undiscovered theft and unregistered Supply Points are not an SSP only issue and it would appear equitable for LSP Users to contribute to industry costs in these areas. As such we support the principle of the LSP market making such a contribution.

However, the nature of these 'losses' makes any precise quantification of the full extent of the impact impossible to calculate.

To inform our response, we have identified two of the main areas for energy losses and provided evidence, where available, relating to the impact and respective volumes attributable to Smaller and Larger Supply Points.

1. Undetected Theft

Theft that occurs upstream of the Emergency Control Valve (ECV) is the responsibility of the Transporter and an assessment of the level of such is included in the shrinkage allowance funded by the Transporter. In the event that this assessment is misstated, the error will effectively pass to RbD. This potential shortfall/surplus is not accounted for within RbD Verification.

Conversely, the cost of theft that occurs downstream of the ECV is a User responsibility. Where this theft is undiscovered, the cost is levied to the SSP Users via RbD. By definition, undetected theft can only be estimated and one potential method of informing an estimate of each market sector's proportion of such is to review the detected instances. RbD Verification makes an allowance for theft downstream of the ECV but any additional theft will contribute to any breach of the Verification tolerance described below.

Current theft figures are shown below:

	2006
Number of suspect incidents reported	3,928
Number investigated	3,995
Actual confirmed cases	1,379
LSP	17
SSP	1,362
Volume of gas estimated	33GWh
LSP	3GWh
SSP	30GWh

These figures suggest that discovered theft runs at approximately 0.02% of Supply Points, contributing approximately 35GWh of energy annually; all of which is currently invoiced to the SSP market. The figures previously provided to the UNC Distribution Workstream illustrate that where theft is discovered at an LSP, it is of a large volume. Although LSP theft accounted for less than 2% of the discovered Supply Points it was 9% of the volume.

2. Unregistered Sites

Liability for the costs of gas consumed by Supply Points that do not have a Registered User are met by the SSP Users via RbD. RbD Verification does not take account of such and may also contribute to any breach of the Verification tolerance.

Current unregistered Supply Point statistics identify approximately 69,000 unregistered Supply Meter Points for the last three years, of which around 2% are LSP. The AQ for unregistered Supply Meter Points is generally unreliable but if an average AQ of 20,000 KWh for SSP and 170,000 KWh for LSP were assumed, this would amount to 1.6TWh of energy currently invoiced to the SSP market where 0.2TWh should be within the LSP market (12% of the total). These figures are in line with those for discovered theft suggesting between 9 and 12% of the energy currently within the SSP market for these issues should more correctly be invoiced to the LSP market. Historically, Verification carried a 0.25TWh allowance for unregistered Supply Points until this was removed twelve months ago.

A concern with both of the above calculations is that they rely on approximations and are arguably not reliable enough to be a basis for invoicing. However, they do indicate some support for the basic argument and indicate that the share of the reconciliation which is attributable to LSPs is between 9% and 12%.

RbD Verification

Verification analysis uses a sample of domestic customers who read their Meters on a weekly basis, thus providing accurate consumption values for the sample. The sample is statistically valid and as a stratified sample covers the full range of consumers within the SSP market. On a monthly basis, consumption from the sample is used to estimate an average consumption per SSP customer. This is compared with commodity and reconciliation invoices to produce a difference value.

As Verification uses a sample, there is a tolerance within which any difference between the sample and the actual invoices may be sampling error. This tolerance is approximately 1% on a national level, slightly higher at an LDZ level. While the difference remained below the 1% level, Verification provided evidence that the charges through RbD were equivalent to those that may have been expected with Individual Meter Point Reconciliation. However, for a number of years the difference has been increasing month on month and is now outside of the tolerance. This suggests that SSP Users have been invoiced more through RbD than their customers have consumed.

Overall verification currently suggests that once all the issues and bias in the sample have been taken into account, there is an outstanding 41TWh of energy (approximately 1.19 % of SSP throughput) that has been invoiced to the SSP market that cannot be explained. This is outside the tolerance of the analysis and suggests that there is an element of energy within RbD that either has not yet been explained, or should not have been billed to the SSP market, or identifies a shortfall of meter points in the SSP sector. The analysis cannot determine which of these the true case is.

Modification Proposal 0115A

Modification Proposal 0115A proposes that Daily Metered (DM) Supply Points and all Monthly Read Meters should be exempt from the reconciliation smear identified within Modification Proposal 0115. The Proposer justifies this based on read rates being high within the above 293,000 kWh market and activity such as theft and unregistered Supply Points are unlikely. Whilst there is insufficient evidence to confirm or deny the claim relating to theft, there have certainly been cases of unregistered Supply Points with Annual Quantities (AQs) above the 293,000 kWh threshold.

The Proposer claims that they achieved a Monthly Read success rate of 99.5% of their Monthly Read Meters. However, calculation of the current national portfolio shows that just under than 10% of the Monthly Read LSP population have not been read within the past 4 months, some 14,300 Supply Meter Points from a population of 147,500 Monthly Read Meters.

In terms of read performance, the most recent information presented to the RbD Sub-Group reviewing this area illustrated that although the average read period for a monthly reconciliation (based on Monthly Read Meters) was 49 days, there was a significant spread of reconciliation up to 200 days. Although this shows a peak at the expected thirty days there is a wide spread with a second peak at 60 days. Our estimate suggests that 70% of Monthly Read Meters are read regularly – i.e. every month.

The Proposer argues that performance is much better in the Monthly Read sector than for Annual Read Meters. Analysis completed at the same time for Annual Read Meters shows that there is a wider spread of periods. The expected days for reconciliation in this category would be 180 days if Users read six monthly, or 365 days if Users meet the Annual Read frequency required within the UNC. The average was 172 days with many actually being read more frequently. These statistics challenge the Proposers assertion that read performance is much improved within the Monthly Read sector.

We are concerned that UNC TPD Section M 3.1.7(b) permits the 'election' of any Supply Meter Point >73,200 kWh to be Monthly Read. In theory, any User wishing to avoid any exposure to the reconciliation smear could renominate all of the LSP NDM Supply Points within its portfolio to be Monthly Read Meters. Given that LSP Users have expressed specific concerns within the UNC Distribution Workstream relating to the unquantifiable

financial risk associated with the proposed RbD smear, we believe that LSP Users are likely to favour the fixed costs associated with procurement of 3 reads per year under TPD Section M3.4.1 (despite Users being required to procure reads for such Meters on a Monthly basis). This therefore provides an incentive to elect LSPs as Monthly Read to avoid the uncertainty associated with RbD.

We also believe that this could also give rise to a risk of a substantial increase in 'must reads' being required to be procured by DNOs in accordance with TPD Section M3.6.

In an extreme case, if a significant proportion of NDM LSPs were 'elected' as Monthly Read Meters, the existing financial exposure to the SSP community would not be diminished and ultimately the Modification Proposal rendered ineffective. We also question the logic that immediately upon a Supply Meter becoming Monthly Read, it is by definition exempt from the reconciliation smear.

We do not believe that this risk can be countered by, for example, removing the 'elective' provision from the UNC as we believe the use of this is likely to increase in any event with the advent of Smart Metering. Further, we note that the purpose of the Monthly Read 'elective' provisions is to provide a genuine opportunity for Users to submit an increased volume of Meter Readings to Transporters' for example to facilitate timely Individual Meter Point Reconciliation. Our view is that Users may be incentivised to undertake such elections simply to avoid the reconciliation smear.

Transportation Rates

Modification Proposal 0115 proposes that the reallocation smear to LSPs is charged at SSP rates. Within the LSP sector there are multiple rates by End User Category (EUC). For Supply Points with an AQ of 732,000 KWh and above, the rate is based on peak off take (SOQ) values and varies with each Supply Point. Charging for RbD does not have this complexity as there is a single rate for the whole SSP market.

The Proposer argues that the wider smear is more appropriate for issues such as theft and unregistered Supply Points. In both cases it is not possible to identify within which EUC the energy is being consumed. This makes the setting of multiple rates difficult and appears to rule out any option other than a standard rate. Multiple rates would require a significantly more expensive invoicing solution within xoserve. From a system cost perspective a single rate would be beneficial for Transporters in decreasing development costs.

Beyond the ease of implementation, there is limited logic in using the SSP rate, other than precedents set by the Modification 640 reconciliation, although from a Transporter perspective in transportation charge terms, Transporters would be neutral to the process. Any lower rate from within the LSP market as advocated by Modification Proposal 0115A would have a short term impact on the Transporter's income which could be resolved through rate changes via the 'K' factor.

Summary:

In respect of Modification Proposal 0115, in our opinion there is sufficient evidence that arguments in favour of LSPs bearing a proportion of the RbD reconciliation smear have foundation. However, whilst the evidence suggests that LSPs are responsible for a quantity of missing energy, it is difficult to accurately assess the proportion of such (relative to that attributable to SSPs). The support from RbD Verification is based on a sample and there are few other robust data sources to provide quantitative evidence.

Based on current NDM AQs, the volume of energy which the Proposer seeks to reallocate through Modification Proposal 0115 to LSP Users would be approximately 40% of the reconciliation volume. In our opinion this would seem to be excessive in light of the proportion (in volume terms) of identified theft occurring downstream of the ECV and unregistered sites. It is on this basis that we strongly qualify our support.

For the reasons described above, we do not believe that the arguments in favour of Modification Proposal 0115A are robust. More specifically, we believe that the likelihood that Users will wish to renominate LSPs to become Monthly Read to avoid any reconciliation smear will render the Modification ineffective or as a minimum create further uncertainty for SSP Users.

We trust these comments will be useful for compilation of the Final Modification Report.

Please contact Chris Warner on 01926 653541 (chris.warner@uk.ngrid.com) should you require any further information with respect to the above.

Yours sincerely

Phil Lawton
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