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Dear Julian,

RE: Modification Proposal 0152V / 0152AV / 0152VB: "Limitation on Retrospective Invoicing and Invoice Correction"

Thank you for the opportunity to comment on these proposals

As the proposer, British Gas Trading (BGT) believes that all three proposals better facilitate the relevant objectives to a greater or lesser extent. Of the three, we would rank our support as follows:

- 0152V (5 year model) - best facilitates the relevant objectives
- 0152VB (6 year model) - better facilitates the relevant objectives but to a lesser extent than 0152V
- 0152AV (7 year model) – better facilitates the relevant objectives but to a lesser extent than 0152V or 0152AV

Background

British Gas Trading sought to establish a UNC Review Proposal in order to facilitate a thorough industry discussion on the difficulties posed by the current regime, which allows an open ended time period for invoice adjustments. These difficulties have been well aired, especially recently in the light of the Farningham NTS-LDZ offtake meter error, but in summary have resulted in millions of pounds of unexpected costs being recharged by Transporters to Shippers.

Membership of the Review Group was open to all Shippers and Transporters, as well as being attended by xoserve, who provided significant industry data on this subject.

Cost shocks are never welcome in business, and especially when they are of the magnitude and frequency seen in recent years in relation to Transporter meter errors. Such errors have tended to span a number of years, and an intrinsic element of the Review Group was to understand how incentives on Transporters with respect to ensuring meter accuracy could be increased in order to limit the scope for further such incidents. In addition to offtake meter errors, the Review Group considered whether it was appropriate for any invoice retrospection limitation period to encompass events other than offtake meter errors.

Following discussions spanning six months, the Review Group charged with looking into these issues arrived at a position where the consensus of attendees was that the UNC should contain a limited period, which would roll forward annually on 1st April. Further, the majority of attendees supported a fixed close out period known as the “5 year model”, which would span a period of 4 years and 0 days, up to 4 years and 365 days. As noted in the Review Group report, however, the NTS Shrinkage Manager expressed a preference for a 6 year model, but the report also states that “*this period can be reviewed at a future date in the light of experience*”.

Having reviewed the evidence presented to the Review Group by xoserve, and having listened to and understood the views of the majority of attendees, BGT raised proposal 0152 (later varied to 0152V for the purposes of adding clarity). BGT believes that 0152V best captures the views expressed by Review Group 0126 attendees.

Modification 0152V

Evidence presented by xoserve to Review Group 0126 demonstrates that after a period of 4 years, the vast majority of energy consumed within the industry has been correctly reconciled, and the benefits of a longer close out period for retrospection diminish after this time. It must also be recognised that some energy will never be fully reconciled due to theft, portfolio issues etc, therefore waiting for full energy reconciliation before invoice close out is impossible. Whilst it is evident that to a degree the longer the period, the more energy will be reconciled, a pragmatic view needs to be taken about the degree of additional energy reconciled over time, against the increased risk to Shippers from delaying a close out period.

A significant element of the Review was to ensure that Transporters had appropriate incentives to undertake thorough NTS and LDZ meter accuracy verification on a regular basis. BGT believes that the lack of such incentive in the current UNC, by virtue of the open ended charging regime, has played a significant part in the magnitude of the historic meter error charges. Again, BGT believes that setting the invoice close out period to the 5 year model will provide a significantly greater incentive to close out these issues than currently exists.

Clearly different parties may take different views on the appropriate period of time for invoice close out, however BGT believes that 0152V strikes the right balance, and believes that this view is supported by the majority of Review Group 0126 members.

0152V also ties into the 5 year price control more closely than the other proposals, thereby giving greater clarity to all Users on incentives, and allowing better cost reflectivity.

Alternative proposals

Two alternatives to 0152V have been proposed. As far as BGT is aware, these are essentially identical to 0152V albeit they seek to establish different time periods for retrospection. 0152VB proposes a “6 year model”, whilst 0152AB proposes a “7 year model”.

As noted above, the NTS Shrinkage Manager was a notable exception to the support for the 5 year model during Review Group discussions, instead preferring a 6 year model. BGT agrees that it is helpful for this alternative proposal to be available for wider consultation and consideration by Ofgem when arriving at a decision.

0152AV proposes a 7 year model. The membership of Review Group 0126 did not identify this period of retrospection as being particularly relevant, and it was therefore not subject to the same degree of scrutiny as the 5 year and 6 year models. Similarly, Review Group 0126 made no recommendation in respect of the 7 year model.

BGT understands that the basis for 0152AV is the concern over the apparent mis-match between the proposed 5 year model, and the Statute of Limitations, which allows for contractual claims to be made for a period of up to 6 years in England and Wales. BGT's understanding of these concerns is that this could give rise to Shipper exposure to customer claims, which are not then backed off by a similar period for counter claim against Transporters.

BGT cannot agree with this thinking. First, contract law as it applies to energy supply contracts in the non-domestic sector permits parties to a contract to agree to any such period for invoice closure as they deem appropriate in any given circumstances. BGT therefore believes that any Shipper concerned about such exposure to a customer claim could mitigate their risk through their supply contract terms and conditions.

Secondly, leading on from this point, we would highlight that the industry has already experienced a situation where, in the circumstances set out above, Shippers would have been fully exposed to customer claims without recourse to the Transporter, for a period of 6 years. This would have occurred at the conclusion of the IQR process. In that case, the industry agreed that all invoicing claims were closed out as a full and final settlement with effect from 1st February 1998. However, this action by the industry would not automatically have restricted a customer's ability to recover costs from a Shipper.

In the absence of evidence suggesting that Shippers were harmed by customer claims under these circumstances, BGT would question whether this is in fact a material issue, even if a Shipper felt unable to amend their supply terms and conditions to neutralise any perceived risk.

BGT also believes that a period of 6-7 years would dilute the incentives upon Transporters to ensure NTS and LDZ meters are operating correctly compared to the current UNC

baseline. Indeed, it was stated as part of the Farningham discussions that the period over which the Farningham meter under-recorded was about as long as it was possible for any meter error to go undiscovered.

Had the proposed 7 year model been in effect prior to the Farningham error being discovered, it would have made relatively little difference to the final charges eventually levied. BGT therefore believes that the 7 year model fails to deliver any material increase in Transporter incentive in this respect, which was a cornerstone of the 0126 Review.

BGT understands that whereas there is a six year limitations period in England and Wales, the equivalent period in Scotland is 5 years. To the extent that there is a mismatch between 0152V and the six year limitations period in England and Wales (which we believe can be mitigated through supply contract Terms and Conditions), this also suggests that 0152V would tend to align with the limitations period in Scotland. Further, this would suggest that for customers supplied in Scotland, the 7 year model goes significantly beyond what is necessary if a User were to rely solely on a limitations Act rather than contract Terms and Conditions.

Relevant objectives

BGT considers that all of these proposals better facilitate the relevant objectives to a greater or lesser extent.

A11.1 (a) The economic and efficient operation of a pipeline system

A key consideration for Review Group 0126 was to increase incentives on Transporters in respect of ensuring NTS and LDZ meter accuracy. More accurate metering will lead to a better understanding of the energy flowing through the pipeline system, allowing more appropriate balancing actions. This will better facilitate the achievement of a more economic and efficient operation of a pipeline system. This will also lead to an increase in User confidence in such metering systems.

By setting the shortest period for retrospective invoicing out of the three proposals, 152V provides the strongest incentive on Transporters to provide accurate metering systems and processes. We therefore consider that 0152V best facilitates this objective. Of the two alternative proposals, we consider that 0152VB – with its six year model – provides the second strongest incentive with 0152AV providing the weakest incentive of the three.

A11.1 (b) The co-ordinated, efficient and economic operation of (i) the combined pipeline system and/or (ii) the pipeline system of one or more other relevant gas Transporter

BGT believes that, to the extent that these proposals incentivise Transporters to ensure metering systems are operating accurately, the proposals will also ensure closer co-operation between Transporters with respect to the meter accuracy verification. The greater the incentive on accurate metering, the closer BGT believes Transporters will coordinate their efforts. Therefore, by setting the shortest time period, 0152V will best facilitate this objective.

A11.1 (c) The efficient discharge of the Licensee's obligations under this licence

Accurate metering is essential to inform Transporter decisions in respect of efficient system investment, system balancing, and security of supply. BGT believes that as this 0152V best incentivises more accurate metering, which in turn should assist Transporters in taking better decisions.

A11.1 (d) The securing of effective competition between relevant shippers

Under the current regime, errors such as Farningham result in a smear of costs across Users, rather than strictly accurate charges targeted at those who incur them. Reducing the period over which costs can be recovered will reduce the extent of any future cost smear across Shippers. The shorter the time period, the lesser the extent of the smear. Therefore, BGT believes that 0152V best facilitates this relevant objective in this regard.

A11.1 (f) – the promotion of efficiency in the implementation and administration of the Uniform Network Code.

Requiring xoserve to hold less data will lead to lower costs. The shorter the period of time over which data needs to be held, the lower xoserve's costs will be. Xoserve will not need to retain data beyond the UNC cut off period (for example it will not need to retain data up to the six year Statute of Limitations cut-off period), as all xoserve related transactions will be subject to the time restriction in the UNC.

BGT believes that by setting the shortest time period, 0152V delivers the largest possible cost saving.

Summary

BGT believes that as a result of Review Group 0126, there is a strong mandate from the industry for implementing limitations on retrospective invoicing under the UNC. Further, that Group concluded by majority that the 5 year model put forward by 0152V was the most appropriate, given the key considerations of energy reconciliation, Shipper uncertainty, and Transporter incentives to provide accurate metering. BGT therefore fully supports the implementation of 0152V.

Of the two alternative proposals, BGT can see a diminished case for 0152VB, but believes that whilst 0152AV may better facilitate the relevant objectives compared to the current UNC baseline, the case in support of its implementation is significantly weaker than for 0152V, and 0152VB.

Should you have any queries with regard to this response please do not hesitate to contact me.

Yours sincerely,

Chris Wright
Commercial Manager