Questions/Problems - Mod 277 draft Mod Report

1. At this stage I don't believe the modification is sufficiently developed…There are a number of significant issues still to be addressed:

- Principles for "windfall avoidance scheme" are not sufficiently developed
- Classification of a valid theft for the allocation of a credit within the scheme is not defined which could lead to differentiated treatment of customers by suppliers who are trying to maintain a performance level in the scheme.

2. The ERA/ENA report recommendations stated that "**incentives MAY provide a more appropriate economic incentive**". [1] The report further recognised that smaller parties would be disadvantaged by an incentive regime, and that there are major demographic differences between suppliers that would disadvantage suppliers with more of a rural customer base.[2]

3. Review Group UNC0245 – Only one supplier supported the further development of the proposal, the remainder preferred the development of an alternative solution – the National Revenue Protection Service.

4. The Lack of Incentives – doesn't give rise to 3 significant issues….It is theft that gives rise to 3 significant issues not the lack of incentives.

5. The recommendation of the ERA/ENA work was wider than the introduction of the SETS scheme and actually refers to multiple schemes across gas and electricity.

6. The Mod UNC-245 workgroup that met with xoserve identified that there is not an equal assessment of" valid theft" by all parties, with some suppliers applying a more hard-line approach to classification of the investigation as valid theft.

7. Market share approach is flawed – xoserve conducted research into valid thefts notified to xoserve and determined that there was a more geographical basis to theft which supports the pros and cons of incentive schemes in the ERA/ENA work, and the ERA/ENA report also reached the same conclusion. *(See footnote 2)*

8. SETS is the Supplier Energy Theft Scheme. The UNC is a Shipper/Transporter code. It could be argued that governance of a supplier scheme is not appropriate in the UNC.

9. Market Share measurements. Depending on a number of issues during the year of the scheme – there may be shifts in market share during the annual period of the scheme, which can have an impact on the final determination of any payments from the scheme.

10. RbD – stated as Resolution by Difference in page 2, bullet point 2, the correct term is "Reconciliation by Difference".

11. The NRPS scheme will not require incentives on suppliers to make it effective, therefore this reference to Mod 274 is inaccurate.

---

[1] The summary of recommendations page 3 of the ERA/ENA Report of the Theft Working Groups 2006

[2] Pg 68 of the ERA/ENA report 2006.

12. The Incentive scheme cannot guarantee that it will lead to an increase in the amount of theft detected. Since no-one knows exactly how much theft is occurring on the networks it is impossible to guarantee an increase in theft detections based on the introduction of an incentive scheme, at best it should state that the proposer believes it will lead to an increase in the amount of theft detected.

13. The principles of the incentive scheme:

1. Market share measurements only taken on D365 – does not consider what movement may occur in market share during the year.
2. Details of what is "valid" theft for credit in the scheme are not yet defined.
3. How do thefts occurring across suppliers count – e.g. if a supplier begins an investigation but is prevented from completing it due to the customer change of supplier and new supplier completes the activity?
4. Who will agree the transporters costs for administering the scheme, how will these be apportioned, single charge for each theft reported to the scheme or by market share?
5. What is the agreed level of evidence to support a claim?
6. Is it the intention that the scheme will be fixed in future at the value of £8.7m or will it have to be revised as supplier's spending increases on revenue protection activity, and if so, how is it envisaged that this figure will be validated?

14. The windfall avoidance proposal by BG – whilst very much appreciated, more information is needed on how this will work.

1. What is the proposed capped amount?
2. Does this capped amount create a protection for BG for the amount they are required to contribute to the scheme?
3. How will the roll forward amount be treated - will BG be entitled to compete for a share of it (i.e. rolled into the scheme's total fund or will it be protected and available only to other participants.
4. What will happen to the amount rolled forward at the end of year 2, will that be ring fenced in the year 3 scheme and unavailable to BG?

15. Benefits –

1. Suppliers already have an incentive to detect theft – loss of revenue and the impacts on RbD.
2. Suppliers don't "do nothing", as a minimum suppliers respond to their conquest notifications and will not ignore unsafe situations reported to them by the public or by their agents. The proposer may feel that suppliers don't do enough – that is not the same thing.
3. There is a counter risk that by the introduction of a further financial obligation on parties to contribute to the SETS scheme as well as fund additional revenue protection activity – that the costs v benefits of contributing to the scheme may well lead to parties choosing to do nothing, other than contribute to their share of the fund. If it costs them to do something as well as to do nothing – the cost to do nothing may well outweigh the cost of doing something!
4. The Scheme must apply equally to non-domestics as well as domestic sites, since the volume of theft in the non-domestic sector potentially has a greater impact on energy balancing and RbD.
5. The scheme is not self financing. Parties will be required to find an investment each year of the schemes value – parties may be able to recover their share of the fund, but they cannot ensure that any portion of their contribution is returned, therefore parties may be required

to continually invest a sum of money along with increased costs of RP activity without the ability to determine how successful they are, so while the scheme may pay out its costs and benefits to the participants in proportion to their success or otherwise, individual parties may have to fund on-going costs without any guarantee of returning value.

This money is therefore used inefficiently, as a supplier I have to provide for this money to be available to the scheme, and this is a cost to my customers. I cannot determine my individual success in the overall scheme and so my investment is 100% at risk. At the end of each scheme year, I am required to find a similar amount and again, therefore even if I get my full contribution back – I have to put it back into the scheme, therefore there is a cost that delivers no benefit to my customer.

16. Consequences of non- implementation – There is a risk with this proposal that it will push up the cost of revenue protection activity to supplier's businesses which will result in increased costs being passed through to customers, with no guarantees that additional theft will be found by each supplier since both xoserve and the ENA/ERA report concluded that theft detections do not follow market shares.

Those suppliers with niche portfolios or with a more rural customer base will face increased costs to fund a scheme from which they may have little chance of realistically seeing their contribution returned at the end of each year; furthermore they will have to resource a RP service that may have little hope of finding theft and therefore further increase their cost base. This may result in niche parties being unable to absorb those costs and this may affect their competitive position in the market.

17. Costs – What about the upstream theft that suppliers find through their investigations?

18. Relevant objectives –

An incentive scheme does not guarantee to find more theft – parties may choose to pay into the fund and not carry out any additional activity, relying on the current industry reporting processes and their current detection activity. The assertion therefore that there will be less unsafe situations on the networks cannot be proved, nor that the incentive scheme will find those unsafe situations more quickly, since customers who steal are usually doing whatever they can to prevent access to sites or to reinstate legal/safe connections when sites are visited.

The consequences of the introduction of the scheme could just lead to an increased cost burden on customers and not an increase in theft detection. It could lead to the upward spiralling of investigation costs without a proportionate cost recovery, leading to a less efficient use of resources.

If the mod expects to deliver an increased detection level of upstream theft then transporters should be included in some way too.

Improvements to competition – we believe this will disadvantage parts of the market and will actually distort competition by creating a requirement for increased costs on parties with no surety of value return.

Gas Demand – there is no evidence presented to the group that incentives will lead to the finding of more theft – therefore the claims that it will enable better forecasting of seasonal gas demand is stretching things!