

Stage 01: Modification

0429:

Customer Settlement Error Claims Process

At what stage is this document in the process?

- 01 Modification
- 02 Workgroup Report
- 03 Draft Modification Report
- 04 Final Modification Report

This modification creates a claims process that will allow Shippers to correct settlement errors for the period after the close out of reconciliation up to the statute of limitations.



The Proposer recommends

The modification is referred to a Workgroup for Assessment



High Impact:

Suppliers, Shippers, Customers



Medium Impact:



Low Impact:

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About this document:

This document is a modification, which will be presented by the Proposer to the Panel on 21 June 2012. The Panel will consider the Proposer's recommendation, and agree whether this modification should be referred to a Workgroup for assessment.



3 **Any questions?**

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1 Summary

Is this a Self-Governance Modification

This modification will have a material impact on Shippers when approved, so is not suitable to be considered under the Self-Governance Process.

Why Change?

At present the UNC limits all retrospective invoices to a period between 4-5 years, depending on when the invoice is triggered. This creates a mismatch between the current reconciliation window and the Limitation Act that governs all contracts, allowing invoices to be queried and adjusted if necessary for a period up to 6 years from the time of action. This means that any energy invoices between Shippers and Customers that are adjusted for the full period allowed under the Limitation Act cannot be fully reflected in energy allocation in settlement under the current UNC processes. On a case by case basis, this could also lead to legal action between Shippers and Transporters where a Shipper has been charged for energy and transportation that it has not used.

Solution

The proposed solution to the problems identified above is the creation of a claims process for Shippers to use when major loss is incurred in the gap between the end of the reconciliation window and the Limitation Act.

The AUGE process may require a separate change through amendment of its guidelines statement to address the impact of a shorter reconciliation process than the Limitation Act and the creation of the proposed claims process. Any such change will be through a separate process under the change procedures for the AUGE Guidelines Statement.

Impacts & Costs

The AUGE assessment of any mismatch between the reconciliation period and the Limitation Act will provide increased certainty that costs are being allocated correctly. Providing a settlement error claims process up to the Limitation Act period will reduce the financial risk exposure currently facing Shippers. In particular this would give added protection to smaller Shippers that could otherwise be made financially unviable by a mismatch between the Limitation Act and the reconciliation period.

It is envisaged that, if central systems changes are required to support this modification, this will be a User Pays Modification.

Implementation

- 01 October 2013 if a decision is received prior or on 01 April 2013
- 01 April 2014 if a decision is received after 01 April 2013 and prior or on 01 December 2013
- If a decision is received after 01 December 2013 implementation should be on the following 1 April that is at least 6 months after the decision date.

The Case for Change

The current processes do not recognise the mismatch between the Limitation Act and the UNC reconciliation period. Recognising this mismatch through a claims process will, first, reduce the risk that Shippers have no option but to take legal action against the Transporters in order to recover unavoidable losses incurred outside of the reconciliation period and, second, will ensure that costs are more accurately targeted.

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As the risks from the mismatch in periods are often unpredictable and beyond a Shipper's control, but with potentially large financial consequences, the inclusion of a claims process will help ensure that smaller Suppliers and Shippers that are least able to manage such large and unpredictable risks are not unduly disadvantaged, thereby helping to reduce barriers to entry and facilitate effective competition.

Recommendations

As this modification is relatively simple in nature the proposer recommends that this modification goes for assessment at a Workgroup for a short period of time.

2 Why Change?

Mismatch between Limitation Act and UNC reconciliation window

The Limitation Act 1980 limits the enforcement of commercial debt to a period of six years. Furthermore, the effect of Unfair Contract Terms Act 1977 is such that it will prevent Shippers from contractually aligning their and their customer's cost exposure to the timescales of the UNC process when a clear settlement error has occurred. Standard contracts are usually used which means any ability to limit a customer's time to pursue a claim will always be subject to a test of reasonableness which by its very nature will depend on the circumstances in each case. This means that there is currently a gap between the period for which a Shipper or customer can claim back costs incurred under their commercial arrangements, and the period for which settlement accommodates this correction.

In the event that an over-recording of customer consumption is identified, this mismatch in time limits leaves Shippers exposed to repayment of costs to their customers that they are unable to back off in settlement, with the full amount of gas initially, and inappropriately, allocated to that Shipper remaining unchanged. Conversely, when a customer's energy consumption is found to have been under-recorded, then the Shipper is unable to reflect this in settlement, so potentially gaining a windfall since the industry is not compensated for the gas that was inappropriately allocated to each Shipper.

The current reconciliation window is mismatched to the Limitations Act by one to two years for a period four to five years ago. This creates a small amount of risk that any adjustment made to a large meter or a large number of smaller meters in the period of the mismatch may create a significant loss. This risk is relatively low for many Suppliers due to the size of the mismatch, the length of time in the past that this exists and the nature of their portfolios. For a few niche Suppliers, with many larger meters, this risk may be more significant since the scale of any adjustment is potentially large.

Were the industry to consider any further shortening of the current reconciliation window then this would have significant impacts on the settlement process and the market in general. For example, if a reduction to a 2-3 year reconciliation time limit were proposed, the amount of energy that will not be reconciled as a consequence would be in the region of 2.5-3.5% of total throughput. This would represent a significant increase over the current 1.5-2.5%¹ that the current 4-5 year time limit results in.

The impact this may have on the LSP NDM market has been shown by the analysis undertaken by Xoserve on UNC Modification 0395/0398 and presented to the industry on 26 April 2012. The following data shows (as of 31 December 2011) shows an estimate for the amount of energy (kWh and £) that may be yet reconciled for those years.

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¹Source: Xoserve presentation to UNC distribution workgroup 26 April 2012.

Calendar Year	Historic Reconciliation Percentage	Unreconciled Estimate of Rec (mWhrs)	Unreconciled Estimate of Rec £000
2007	-4.62%	-187,084	-3,577
2008	-5.98%	-274,455	-5,247
2009	-4.59%	-202,738	-3,876
2010	-2.47%	-138,807	-2,654
2011	-1.85%	-361,009	-6,902

NB: these figures do not reflect potential adjustments for DM sites, which individually would be much greater.

These figures demonstrate that the current cut-off date creates a situation where a Supplier may be unable to easily correct significant, and for a smaller Supplier, potentially business ending errors in settlement.

A claims process would counter this risk as it would allow the Shipper to claim for significant energy and transportation costs where a consumer had made a claim against them for the period outside of the normal reconciliation process (under the Limitations Act) and would avoid the need for legal challenge to correct the error.

Impact on AUGÉ processes

A key finding of the AUGÉ process has been that many aspects of Unidentified Gas are temporary in nature and will eventually be allocated back to an individual shipper through the reconciliation process. The Customer Settlement Error Claims Process will not result in changes to reconciliation and so there seems to be a need to recognise, through the AUGÉ process, that some sources of Unidentified Gas would not be corrected owing to the current reconciliation backstop date.

Interaction with UNC Modifications 0395 & 0398

We are mindful of the fact that there are two modifications at present (UNC Modifications 0395 & 0398) that are seeking to amend the current reconciliation period. This modification seeks to correct a current issue present in the UNC, namely that the automated reconciliation processes prevents a Shipper from fully reflecting in settlement corrections to customer invoices. We therefore believe there is significant benefit for this change under the current market regime. If either UNC Modification 0395 or 0398 were implemented we would expect the size and number of corrections using the proposed process to markedly increase.

Why there is a risk of legal challenge

It has been noted above that the current backstop date impacts how Shippers can recover their costs for incorrect gas allocations that have been corrected with their customer. As we have noted the current reconciliation cut-off date limits how far a Shipper can currently undertake adjustments through system processes, but as acknowledged by Ofgem:

"The reconciliation process is not in itself a remedy for contractual breach but a discrete operational process provided for and operated in accordance with the UNC contract. Where contractual obligations are imposed on parties breaches of these obligations may give rise to contractual claims and the Limitation Act provides that such claims would, as a general rule, have to be brought within six years. This is not affected by the length of time within which reconciliation can occur".

11 October 2007: Ofgem Decision Letter 0152V/AV/VB

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We agree with Ofgem's assessment that Shippers still have the right under contractual law to correct the cost allocation in the event that there has been a clear error. In this case the billing error would sit with the organisation that has undertaken the energy allocation or transportation activity. At present however there is no clear mechanism for this to occur and a Shipper will have to rely on a legal process to correct any significant cost error.

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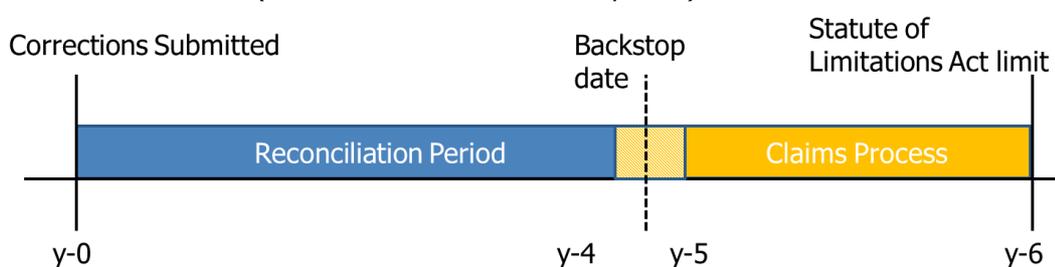
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3 Solution

Settlement Claims Process

To remove the financial exposure that Shippers face as a result of this misalignment, it is proposed that a Customer Settlement Error Claims Process is implemented. This process will allow Shippers, to claim back costs for energy and transportation they should not have been allocated or to submit claims to reflect costs they should have been allocated but weren't. Such claims would be for the period between the Code Cut Off Date and the last Day of Formula Year t-6, as shown below. To ensure only significant adjustments are submitted, it is proposed that such claims would have to be at least £50,000 (energy and transportation) in materiality. The types of claims that could be submitted are those that otherwise would be valid, but have been prevented from doing so due to the Code Cut Off Date.

Illustration of Process (current reconciliation backstop date)



It is intended that this process will be used relatively rarely to correct material errors and will only be used where the nature and materiality of the error can be clearly demonstrated. It therefore will be a relatively manual process with the Shipper expected to submit the claim and evidence supporting the claim to the Transporter's Agent for validation. For the avoidance of doubt, the Customer Settlement Error Claims Process will not impact the period covered by the reconciliation process, concerning itself with the period after reconciliation has closed out.

Initiation of Customer Settlement Error Claims Process

It is intended that this process will be triggered by the Shipper submitting a Customer Settlement Error Claim to the Transporter's Agent. It is proposed that there is a lower limit of total materiality (both energy and transportation components) of the error that cannot be corrected by the normal reconciliation processes of £50,000. The materiality criteria would be applied to an individual Supply Point or a group of Supply Points. In the latter case the error would have to be caused by the same root cause (e.g. error identified with a class of meters or systemic errors with correction factors for a class of customer). These customers can be connected to different networks as the claim is against the system as a whole.

Content of Settlement Error Claim

In addition to this materiality threshold, customer agreement would need to be obtained for any correction (which may mean multiple agreements if a group of customers are impacted). If the error meets the eligibility criteria, the Shipper would be expected to provide to the Transporter's Agent the following:

- Detail on the nature and duration of the error, detailing its materiality in terms of volume of gas as well as an estimate of its financial impact in terms of energy and transportation costs. When determining the cost of the error with regard to energy, it is expected that the Shipper would reference the monthly

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average of the System Average Prices for the period in the claim. When determining the transportation cost, the Shipper would reference the relevant Transportation charges in effect at the time of the claim.

- Description of the issue that caused the error to occur.
- Details of the methodology used by the Shipper to calculate the materiality of the error, including applicable working.
- Copies of invoices between Transporter and Shipper detailing the original costs incurred by the Shipper. This is to allow Xoserve to verify without significant additional work that the Shipper has been incorrectly invoiced in the first place.
- The dates for which the Customer Settlement Error Claim will apply. This will only cover the period after which normal settlement reconciliation closes out, up to the six year limit.
- Written confirmation from the customer(s) that they agree with the Shipper that an error has taken place and the overall materiality of the error, as well as the timescales that the error covers.
- Evidence of the Shipper and customer bills relating to the Supply Point to demonstrate loss.
- Applicable system files detailing the revised charges to be adjusted to allow Xoserve to process the correction and maintain an appropriate record of the correction.

Processing of Settlement Error Claim

Once received, the relevant Transporters would have 90 days to evaluate the claim and either approve or reject it. During that time the Transporter's Agent would have the ability to ask for additional information (in line with the criteria above) to clarify the Customer Settlement Error Claim.

The relevant Transporters will judge the above information on the basis that an average informed person would be able to understand and agree with the calculations undertaken (such as the calculations provided align with the invoicing methodology) to determine the above. Shipper will warrant no previous claims have been made. If the Transporters considers the information provided is so clearly erroneous on its face that it would be unconscionable for it to stand (e.g. a previous claim for the same error had already occurred) then they would be able to reject the claim and inform the Shipper of the reasons why.

For the avoidance of doubt the Transporter will first attempt to resolve any queries it may have with the Shipper, prior to rejecting the claim.

If the Transporter's Agent rejects the claim then the Shipper will have 14 days to notify the Transporter/s that it intends to appeal. Such a dispute will be dealt with by Expert Determination in accordance with General Terms Section A.

The Transporters will be entitled to claim any reasonable costs (time and materials) from the Shipper for the processing of the claim. For the avoidance of doubt this does not cover costs if the determination by the Transporters is disputed by the Shipper, as General Terms Section A covers how costs are handled when the dispute resolution process is used.

Resolution of Settlement Error Claim - Energy Correction.

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In order to preserve the integrity of the settlement process, it is proposed that any energy financial adjustment shall be included in Balancing Neutrality as part of the Monthly Adjustment Neutrality Amount. For the purposes of this process, the value of the Customer Settlement Error Claim will be determined by multiplying the average SAP for the period that the Monthly Adjustment Neutrality Amount will apply by the volume of the Customer Settlement Error Claim. The Shipper will either then pay or be paid this amount as appropriate. Where the Transporters's Agent estimates that charges above £1million are to be applied, the Transporter's Agent will issue a notification to Shippers. In such cases the charges will be applied two months after the Customer Settlement Error Claim is approved.

Resolution of Settlement Error Claim - Transportation Correction.

Any financial adjustment can be taken into account by the Transporters when setting charges for the next financial year.

4 Relevant Objectives

Impact of the modification on the **Relevant Objectives:**

Relevant Objective	Identified impact
a) Efficient and economic operation of the pipe-line system.	None
b) Coordinated, efficient and economic operation of (i) the combined pipe-line system, and/ or (ii) the pipe-line system of one or more other relevant gas transporters.	None
c) Efficient discharge of the licensee's obligations.	None
d) Securing of effective competition: (i) between relevant shippers; (ii) between relevant suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers.	Positive
e) Provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards... are satisfied as respects the availability of gas to their domestic customers.	None
f) Promotion of efficiency in the implementation and administration of the Code	None
g) Compliance with the Regulation and any relevant legally binding decisions of the European Commission and/or the Agency for the Co-operation of Energy Regulators	None

Relevant Objective (d) Securing of effective competition: (i) between relevant shippers; (ii) between relevant Suppliers; and/or (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers.

The proposed process allows Shippers to claim for material settlement inaccuracies that cover the period between the closeout of reconciliation and the Limitations Act.

Reducing risk to shippers will reduce costs to the industry overall and reduce a barrier to entry, and so benefit competition.

5 Impacts and Costs

Consideration of Wider Industry Impacts

No wider industry impacts identified.

Costs

Indicative industry costs – User Pays
Classification of the modification as User Pays or not and justification for classification
User Pays Modification
Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification
100% Shippers
Proposed charge(s) for application of Users Pays charges to Shippers
The charging basis for Shippers will be an allocation of the development costs to each Shipper based upon each Shipper's number of supply points in proportion to the total number of all Shippers supply points as measured on the date of the implementation of the modification, excluding Unique Sites.
Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from Xoserve
To be completed

Impacts

Impact on Transporters' Systems and Process	
Transporters' System/Process	Potential impact
UK Link	None
Operational Processes	Minor changes for the Transporter agent to assess claims
User Pays implications	None

Impact on Users	
Area of Users' business	Potential impact
Administrative and operational	Those wishing to claim would need to establish a process for doing so
Development, capital and operating costs	None

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Where can I find details of the UNC Standards of Service?

In the Revised FMR for Transco's Network Code Modification

0565 Transco Proposal for Revision of Network Code Standards of Service at the

following location:

www.gasgovernance.co.uk/sites/default/files/0565.zip

Impact on Users	
Contractual risks	This process will remove the potential for Shippers to be exposed to costs from customer invoice corrections that could not be backed off by settlement corrections.
Legislative, regulatory and contractual obligations and relationships	None

Impact on Transporters	
Area of Transporters' business	Potential impact
System operation	None
Development, capital and operating costs	None
Recovery of costs	None
Price regulation	None
Contractual risks	Reduction in risk of legal action under Limitations Act if no corrections are made
Legislative, regulatory and contractual obligations and relationships	None
Standards of service	None

Impact on Code Administration	
Area of Code Administration	Potential impact
Modification Rules	None
UNC Committees	None
General administration	None

Impact on Code	
Code section	Potential impact
To be determined by Transporters	<ul style="list-style-type: none">•
	<ul style="list-style-type: none">•

Impact on UNC Related Documents and Other Referenced Documents	
Related Document	Potential impact
Network Entry Agreement (TPD I1.3)	<ul style="list-style-type: none">• None

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Impact on UNC Related Documents and Other Referenced Documents	
Network Exit Agreement (Including Connected System Exit Points) (TPD J1.5.4)	None
Storage Connection Agreement (TPD R1.3.1)	None
UK Link Manual (TPD U1.4)	None
Network Code Operations Reporting Manual (TPD V12)	None
Network Code Validation Rules (TPD V12)	None
ECQ Methodology (TPD V12)	None
Measurement Error Notification Guidelines (TPD V12)	None
Energy Balancing Credit Rules (TPD X2.1)	None
Uniform Network Code Standards of Service (Various)	None

Impact on Core Industry Documents and other documents	
Document	Potential impact
Safety Case or other document under Gas Safety (Management) Regulations	None
Gas Transporter Licence	None

Other Impacts	
Item impacted	Potential impact
Security of Supply	None
Operation of the Total System	None
Industry fragmentation	None
Terminal operators, consumers, connected system operators, suppliers, producers and other non code parties	None

6 Implementation

- 01 October 2013 if a decision is received prior or on 01 April 2013
- 01 April 2014 if a decision is received after 01 April 2013 and prior to 01 December 2013
- If a decision is received after 01 December 2013 implementation should on the following 1 April that is at least 6 months after the decision date.

7 The Case for Change

None in addition to that above.

8 Legal Text

The Transporters are requested to provide legal text in support of this modification.

9 Recommendation

The Proposer invites the Panel to:

- DETERMINE that Modification 0429 progress to Workgroup

10 Appendix one – proposed changes to the AUGE process

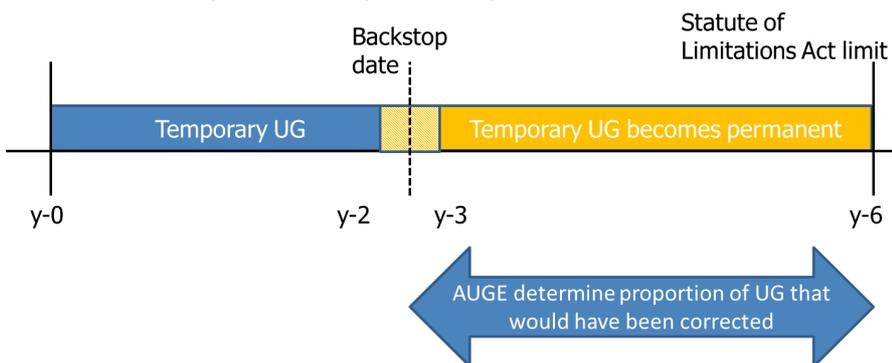
This aspect of the change will be raised as a separate change to the AUGE guidelines statement. It is detailed here in order to give a comprehensive view of the implications of this proposal.

The current AUGE process attempts to determine the scale of Unidentified Gas that is present in the settlements process. A key factor in determining the amount of Unidentified Gas that exists is determining which sources of unidentified gas are permanent (i.e. will never be allocated to an individual Supply Point) or temporary (i.e. will eventually be corrected at some point and allocated to an individual Supply Point).

Shortening the current reconciliation time period will shorten the period in which settlement errors are corrected. It will therefore increase the amount of Unidentified Gas and other energy in the system that cannot be corrected through the reconciliation process and so be classified as permanent Unidentified Gas. The Settlement Error Claim process above will allow for a process to correct settlement errors beyond the reconciliation window, which may include corrections for sources of gas use which would have been originally classified as Unidentified Gas.

It will therefore be proposed that the AUGE should make an assessment of the amount of energy that would have been corrected (and so be classed as temporary Unidentified Gas) were it not for the close out of the reconciliation window. For the avoidance of doubt, this aspect of the change will be raised as a separate change to the AUGE guidelines statement. It is detailed here for the sake of completeness.

Illustration of Proposed AUGE process adjustment.



The AUGE would detail the materiality of this "fossilized" Unidentified Gas and adjust the resulting Unidentified Gas volumes accordingly.