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30th October 2008

Re: Modification Proposal 0194 'Framework for correct apportionment of NDM Error'
Modification Proposal 0194A 'Framework for correct apportionment of LSP unidentified gas'

Dear John,

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

National Grid Distribution (NGD) is able to offer support in principle for implementation of either Proposal. This is on the grounds that the evidence, to the extent that it can be reasonably quantified, suggests that there is an opportunity for energy costs to be apportioned more equitably between Shippers. Both Proposals, whilst not delivering a more equitable apportionment, would facilitate such apportionment in a future Modification. This underpins our belief that the relevant objectives under Standard Special Condition A11.1(d) of the Transporters Licence are better facilitated.

Each Proposal excludes application to Transportation charges and therefore there is no impact on NGD's revenue. However, as a UNC party we have considered, based on the evidence that *is* available, whether one or more of the Proposals represent an improvement on the prevailing arrangements, i.e. whether they *better facilitate* the GT Licence relevant objectives. On the basis that there is evidence that a more equitable apportionment of costs should be facilitated, National Grid Distribution supports both Modification Proposals which are subject to consultation (0194 and 0194A). Unfortunately, evidence of the level of 'unaccounted for' volume is extremely difficult to accurately quantify i.e. it is virtually impossible to determine the extent of unidentified downstream theft hence it is difficult to judge which proposal best facilitates the Relevant Objectives, however we have a narrow preference for 0194A (fixed volume) for the reasons explained below.

Each Modification Proposal identifies a framework containing allocation tables which would govern energy reconciliation settlement. However implementation would not have any effect unless further Modification of the UNC is made given that the tables are either not populated or are done so in a manner that does not change the current position. During industry discussion some parties have argued that the licence objectives are not facilitated due to the nil financial effect. However we do not agree with this view on the premiss that both of the Proposals facilitate future change and are therefore consistent with Standard Special Condition A11.1(f) of the Transporters Licence.

We have participated in all discussions during the development of Modification Proposal 0194¹ and have reviewed all the relevant information that is available. We have also taken the opportunity to discuss each

¹ Modification Proposal 0194 only was subjected to Development procedures.

Proposal with various Shippers which has proven most useful particularly in understanding the effect each may have on end consumers.

It is possible that some of the information provided by xoserve and identified within this representation may appear in other representations submitted.

Background

In September 2006, BGT raised Modification Proposal 0115 which proposed that all RbD energy be smeared across all Non Daily Metered (NDM) Supply Points. The current RbD process allocates primary reconciliation only to Smaller Supply Points (SSPs).

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

Ofgem subsequently rejected Modification Proposal 0115, on the grounds that it did not address the underlying issues behind the perceived imbalance, and because those issues had not been adequately quantified. Following the rejection of Modification Proposal 0115, BGT raised Modification Proposal 0194.

Modification Proposal 0194

Modification Proposal 0194 proposes extending the RbD smear to the LSP market, but with three key differences to the regime identified within Modification Proposal 0115. Proposal 0194 advocates:

- application to energy charges only,
- introduction of an allocation table into UNC Principal Document Section E, which would set out the relative percentage allocations to SSP and LSP market share,
- the inclusion of individual issues within the allocation table such as theft and unregistered sites, based on the size of the issue and the split between SSP and LSP.

As described above, the proposal includes an allocation table which apportions the entire RbD smear to the SSP market. In effect therefore this Proposal is an enabling tool which does not change the existing position. However, later Modification Proposals are facilitated.

Alternative Modification Proposal 194A

Corona Energy has raised an Alternative Modification Proposal 0194A. This proposes creating a table within the UNC to enable a fixed amount of energy to be transferred from SSP to LSP via RbD in monthly instalments. The LSP values are not populated at present. In this respect the Proposal is similar to 0194 in that it would facilitate a later Modification Proposal to populate the table.

Anticipated Impacts on Shippers

Historic trends have shown that RbD charges are typically a debit to SSP Shippers, although the amounts cannot be predicted with any certainty and can vary significantly month on month.

In the event that subsequent Modification of the UNC is achieved resulting in the population of the allocation table with alternative values, a proportion of RbD energy is likely to be smeared to LSP, having the effect of reducing the charge to SSPs. Therefore SSP-only Shippers would in many cases benefit

from the population of the allocation table. LSP-only Shippers would incur additional costs based on their market share of LSP and on the proportion of RbD allocated to LSP

The impact on Shippers with both SSP and LSP market share would depend on their relative shares of the two markets: if their SSP share is larger than their LSP share, they would benefit by the difference in market shares multiplied by the % allocation. Conversely, if the Shipper has a greater share of LSP than SSP, then cost to them would be the difference between their two market shares, multiplied by the % of energy redistributed. Exact impacts cannot be predicted reliably, since they depend on the future trends in primary reconciliation.

Anticipated Impacts on Transporters (including implementation requirements)

Both Modification Proposals exclude transportation charges and only impact the distribution of energy. Therefore there is no direct impact on Distribution Network Operator (DNO) revenues. Given the neutral effect of the both Proposals on the prevailing arrangements in respect of energy charging, there are no implementation costs associated with 0194 or 0194A and hence either Proposal can be implemented with immediate effect. However, in the event that subsequent Modification of the UNC is achieved resulting in the population of the allocation table with alternative values there is likely to be additional processes and costs for xoserve in calculating the additional RbD charges. The extent of this may depend on the system solution and the timing of invoices.

Evidence to support an allocation to LSP Shippers

RbD Verification is one of the key monitors of RbD. xoserve performs this activity every month, comparing the amount billed for SSPs via initial allocation plus RbD against an estimated charge under Individual Meter Point Reconciliation. The analysis uses a sample of British Gas domestic customers who read their meters on a weekly basis, thus providing accurate consumption values for the sample. The sample is geographically distributed and stratified across a range of domestic 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 for an average site. This difference is then extrapolated to an LDZ and national level, which is often referred to as an "imbalance", particularly when the invoiced values are greater than the estimates of meter point reconciliation, as is usually the case.

As RbD Verification uses a sample of Supply Points, there is a tolerance within which any difference between the sample and the actual invoices may be sampling error. At present this tolerance is approximately 1.4% on a national level, slightly higher at an LDZ level. While the difference between invoices and estimated meter point reconciliation remained below the confidence level, Verification provided evidence that the charges through RbD were equivalent to those that might have been expected with meter point reconciliation. However, for a number of years the difference has been increasing month on month and has been outside the tolerance. This suggests that SSP Shippers have been invoiced more through RbD than their customers have consumed.

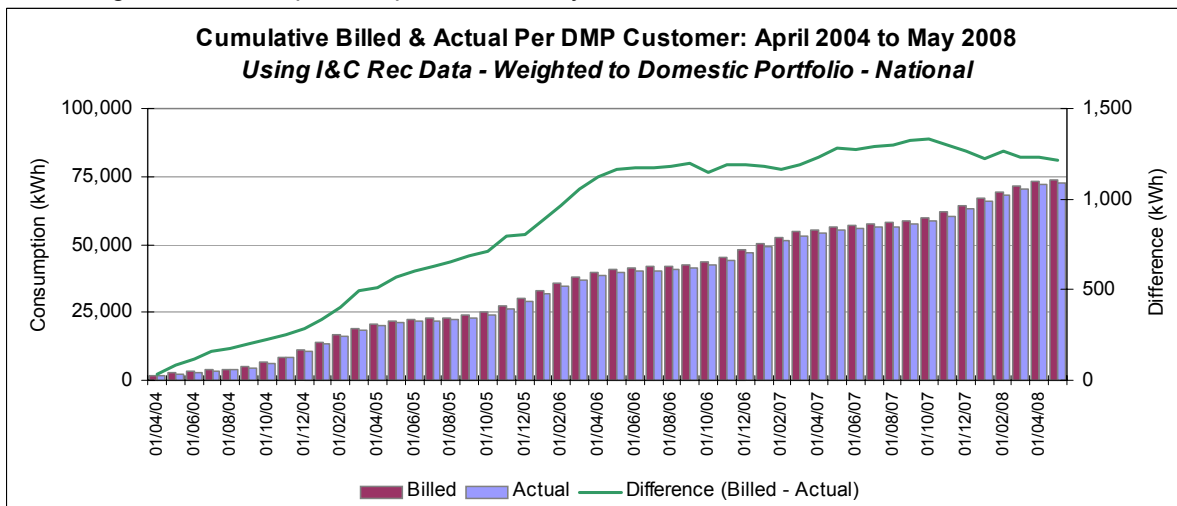
There has been a significant amount of analysis looking at the reasons for this apparent overbill that has produced the additional Verification spreadsheet (below). This spreadsheet takes the raw analysis difference and subtracts from this difference any energy that would be expected to remain in the SSP market but that would not be present within the sample (potential sample bias). The remaining difference is unexplained variation and may be due to an overbill in the SSP market or due to inaccuracies in how each figure is estimated within the analysis.

The table below takes the latest cumulative imbalance for each LDZ for the period April 2004 to May 2008, and estimates the amount of the difference which can be accounted for by various known issues which are not present in the sample population, e.g. theft of gas and threshold crosser sites.

LDZ	Current Balance (TWh)	Theft Of Gas	Threshold Crossers				Shrinkage Adjustment	LDZ Adjustment	Duplicates	Late Confirmed	Inter LDZ Transfers	LDZ Postcode Discrepancy	Postcode Discrepancy 2005	Remaining Balance (TWh)	% Throughput
			(No Adjust) 2004	(No Adjust) 2005	(No Adjust) 2006	(Adjust to Flow) 2008									
EA	2.44	0.49	0.03	0.09	0.03	0.15	0.00	0.00	0.01	0.05	-1.49	3.82	-0.65	-0.08	-0.06%
EM	2.79	0.64	0.04	0.17	0.04	0.18	0.00	0.00	0.01	0.05	-0.03	-0.84	-0.41	2.96	1.78%
NE	2.62	0.39	0.02	0.06	0.02	0.14	0.00	0.00	0.01	0.04	0.00	0.57	-0.25	1.62	1.57%
NO	-0.04	0.35	0.02	0.04	0.01	0.09	0.00	0.00	0.01	0.04	0.00	-0.06	0.21	-0.74	-0.82%
NT	1.98	0.63	0.04	0.13	0.10	0.34	0.00	0.00	0.01	0.11	1.31	-2.30	-1.86	3.46	2.09%
NW	3.89	0.77	0.04	0.13	0.05	0.20	0.00	0.00	0.01	0.10	0.00	-0.12	-0.09	2.78	1.36%
SC	2.49	0.52	0.03	0.10	0.03	0.11	0.00	0.00	0.01	0.03	0.00	-0.33	0.01	1.97	1.44%
SE	0.14	0.70	0.04	0.13	0.06	0.24	0.00	0.00	0.01	0.07	-0.04	-2.33	0.79	0.47	0.26%
SO	4.35	0.43	0.02	0.07	0.03	0.11	0.00	0.00	0.01	0.04	0.22	1.27	1.88	0.26	0.23%
SW	0.31	0.36	0.02	0.10	0.02	0.09	0.02	0.00	0.01	0.06	0.00	-0.01	-0.01	-0.33	-0.36%
WM	1.19	0.55	0.05	0.14	0.04	0.18	-0.01	0.00	0.01	0.08	0.03	-1.09	0.39	0.81	0.55%
WN	2.12	0.06	0.00	0.01	0.00	0.03	0.00	0.00	0.00	0.01	0.00	1.38	-0.01	0.64	3.80%
WS	0.70	0.24	0.01	0.04	0.01	0.06	-0.02	0.00	0.00	0.03	0.00	0.04	0.00	0.29	0.47%
Wales	2.81	0.27	0.02	0.05	0.01	0.09	-0.02	0.00	0.00	0.04	0.00	1.42	-0.01	0.94	0.6%
Total	25.72	6.06	0.36	1.21	0.45	1.91	-0.02	0.00	0.10	0.93	0.00	0.00	0.00	14.71	0.91%

The table shows that the total initial imbalance figure derived from RbD Verification is 25.72 tWh. Once the aggregate value of known issues is subtracted (a total of 11.01 tWh) the remaining imbalance is 14.71 tWh which on average equates to 3.7 tWh per annum imbalance.

The following graph shows the monthly and cumulative national imbalance, before considering any reconciling items, for the period April 2004 to May 2008.



The graph shows a consistent upward trend for the first two years, followed by a flattening off. Since the start of Gas Year 2007/08 the graph shows a net decline in the imbalance. In other words the amount billed via Commodity and RbD is less than the amount estimated as billable via meter point reconciliation for the last Gas Year.

In conclusion, historic RbD Verification analysis indicates that the SSP market has borne the costs of gas volumes over and above that consumed at Smaller Supply Points (known issues having been taken into account). To this extent a more cost reflective model would include apportionment of an element of this gas volume to the LSP market.

Issues Identified within the Allocation Tables

The issues that BGT and Corona raise within their Modification Proposals cover some of those used within RbD Verification. The following table covers each issue in turn, indicating whether it is accounted for within RbD Verification.

Issue	Description	Evidence	Included in Verification	SSP or LSP issue
Read submission issues	The proposer has indicated this represents genuine reconciliation at SSPs	None identified	No	SSP
Unregistered sites	Sites where there is a delay in confirmation after meter fit. Any gas consumed is borne by RbD. If a Shipper who did not originally request the meter fix takes on the site, energy from meter fix to confirmation often becomes stranded in RbD.	See below. Potential 1 tWh p.a. of energy on unregistered sites.	Yes. Includes the energy stranded after confirmation (0.93 tWh) but no ongoing allowance for sites not yet registered.	Although all this energy is paid for by SSP market, there is a case for charging the LSP element to LSP Shippers.
Temp & Press I&C (LSP)	<i>These are two old issues which were formerly in RbD Verification, due to the way that differences in Temperature and Pressure correction on different classes of sites were dealt with. In summary, SSP picked up any difference between national and LDZ corrections, even though LSP was affected. No longer relevant.</i>			
Temp & Press Dom (SSP)				
iGT issues	Understatement of CSEP allocation due to understatement of CSEP AQ	RG 157 figures.	No	Both
LDZ Shrinkage	Any variance between actual shrinkage and the fixed volume allowed is levied to SSPs	Fixed volume set by Ofgem based on leakage studies etc.	Only known amounts, e.g. Annual Shrinkage adjustment, are included	Does not affect LSPs which have reconciled, but affects unread and unregistered sites.
Theft	Unreported or unrecovered theft is all borne by SSP. (Transporter theft is included in Shrinkage, but any errors in the allowance are also borne by SSP).	xoserve statistics suggest 30 gWh of reported theft p.a. of which only 3% is LSP	Yes. 6.06 tWh included, based on historic estimate of 0.4% for theft.	Both sectors affected. Perception that there are more incidents in SSP, but a few high value incidents in LSP.
LDZ Metering	Undetected errors in LDZ input metering	No data available about undiscovered errors	Only known amounts, once announced to industry.	Does not affect LSPs which have reconciled, but affects unread and unregistered sites.
End Supply Metering	Errors in meter reads due to equipment bias	None presented	No	Both.

Further supporting information relating to Theft of Gas and Unregistered sites can be found within Appendix 1.

Application of the allocation tables

It is important to note that although there has been much discussion of the estimated size of the RbD imbalance, that figure is not used in Modification Proposal 0194. The table of percentages is designed to be applied to the whole RbD balance each month. In other words, all primary reconciliation would be aggregated each month and smeared back across SSP and LSP sites in line with the values within the allocation table.

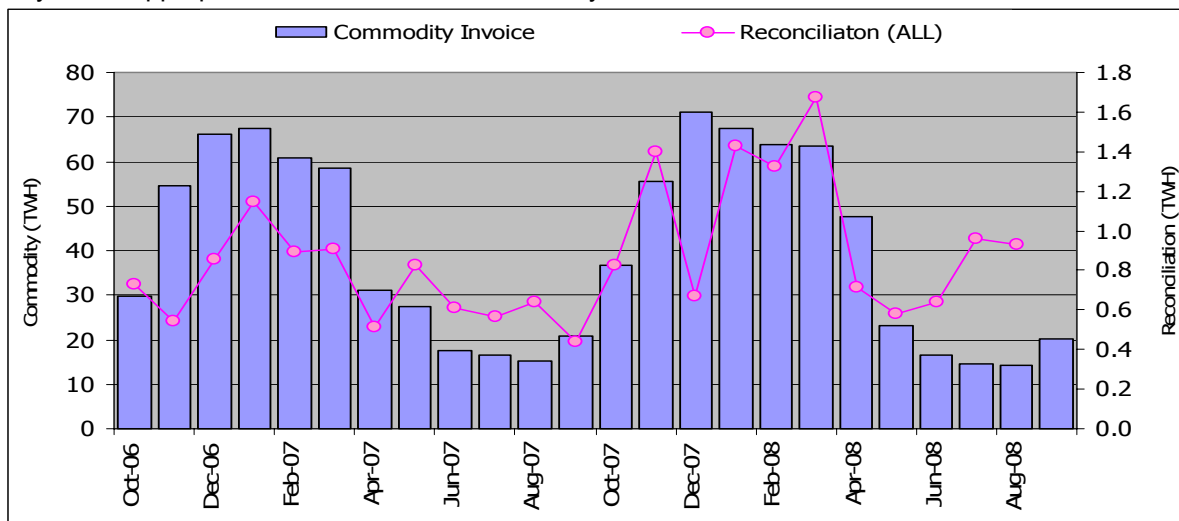
Conversely, Proposal 0194 seeks to enable a *fixed* amount of energy to be transferred from SSP to LSP via RbD in monthly instalments.

Fixed and Variable Volume Allocation

The central premiss of Modification Proposal 194A is that the monthly profile of RbD is not predictable, and does not follow the expected pattern of imbalance energy. Several LSP Shippers have suggested that the energy in the imbalance would not follow a seasonal pattern, and that therefore a fixed monthly charge would be more appropriate.

Our view is that the main known components of the imbalance are Theft of Gas and Unregistered Sites. It is likely but unproven that both of these components could be expected to have a seasonal profile (i.e. have higher values in winter than summer). Both these categories relate to sites behaving normally or perhaps being less concerned than most about gas costs or carbon footprint, because they are not paying for gas, either due to meter tampering or because they do not have a current supplier. However, we believe that these sites would remain sensitive to weather, for example because most SSP and LSP sites use gas mainly for space heating, and therefore require more gas in winter than in summer. Almost all NDM Allocation profiles show a seasonal trend, further supporting the case for weather sensitivity.

The graph below shows the profile of NDM energy allocation for the last two years and the amount of energy flowing into RbD from on-line Primary Reconciliation (on a separate scale, due to the much lower quantities involved). This shows that on-line Primary Reconciliation varies more than Commodity energy, but still exhibits a seasonal trend. This to a limited extent lends some support to the position that RbD may be an appropriate mechanism for the recovery of the imbalance.



There may, of course, be other elements of the imbalance which are not currently identified and which have a different seasonal profile.

Overall Conclusion

The original concept of RbD 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 only holds true if everything is known and all energy is billed correctly. Where there are unknown energy losses, such as through theft or unregistered Supply Points, the 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 in the SSP market.

RbD Verification currently suggests that once all the issues and bias in the sample have been taken into account, there is an outstanding 14.7 tWh of energy that has been invoiced to the SSP market that cannot be explained. Historic patterns of a positive imbalance suggest that either:

- a. there is an element of energy within RbD that has not yet been explained, or
- b. there is an element of energy within RbD that should not have been billed to the SSP market, or
- c. there is a shortfall of meter points in the SSP sector, or
- d. there is a combination of two or more of the above.

The analysis cannot determine which of these the true case is. The imbalance supports to some extent the assertion that smearing the whole reconciliation energy across the SSP and LSP markets is appropriate. However the recent results of RbD Verification, which are within tolerance, and the lack of firm numbers for the reconciling items mean that determining the level of transfer to LSP would be difficult.

In general there are a number of areas where both Proposers appear to have a justifiable argument: theft and unregistered sites are clearly not an SSP-only issue and it would seem equitable for LSP Shippers to contribute to industry costs in these areas. A common theme is that the nature of the issue makes any quantification of the full extent of the impact virtually impossible to calculate. Modification Proposal 0194 does not require this calculation as it seeks to use the reconciliation energy as the basis for the energy re-allocation. The issue of the extent of shared risk is noteworthy. It could be argued that Modification Proposal 0194 provides a mechanism where all unknown risk is allocated.

However, given the level of uncertainty and a lack of robust information to underpin the use of RbD as a basis for a re-apportionment of energy to LSP, we believe the methodology advocated by Modification Proposal 0194A could be more reliable and predictable given its simplicity and transparency.

In conclusion, our view is that on balance 0194A may be an easier mechanism to facilitate a more accurate reflection of cost allocation. We believe that the variations which would potentially arise if the Reconciliation by Difference (RbD) mechanism were used as would be the case under Proposal 0194 would represent less of an improvement over current arrangements than implementation of 0194A. However, we believe implementation of either Proposal would better facilitate the Relevant Objectives.

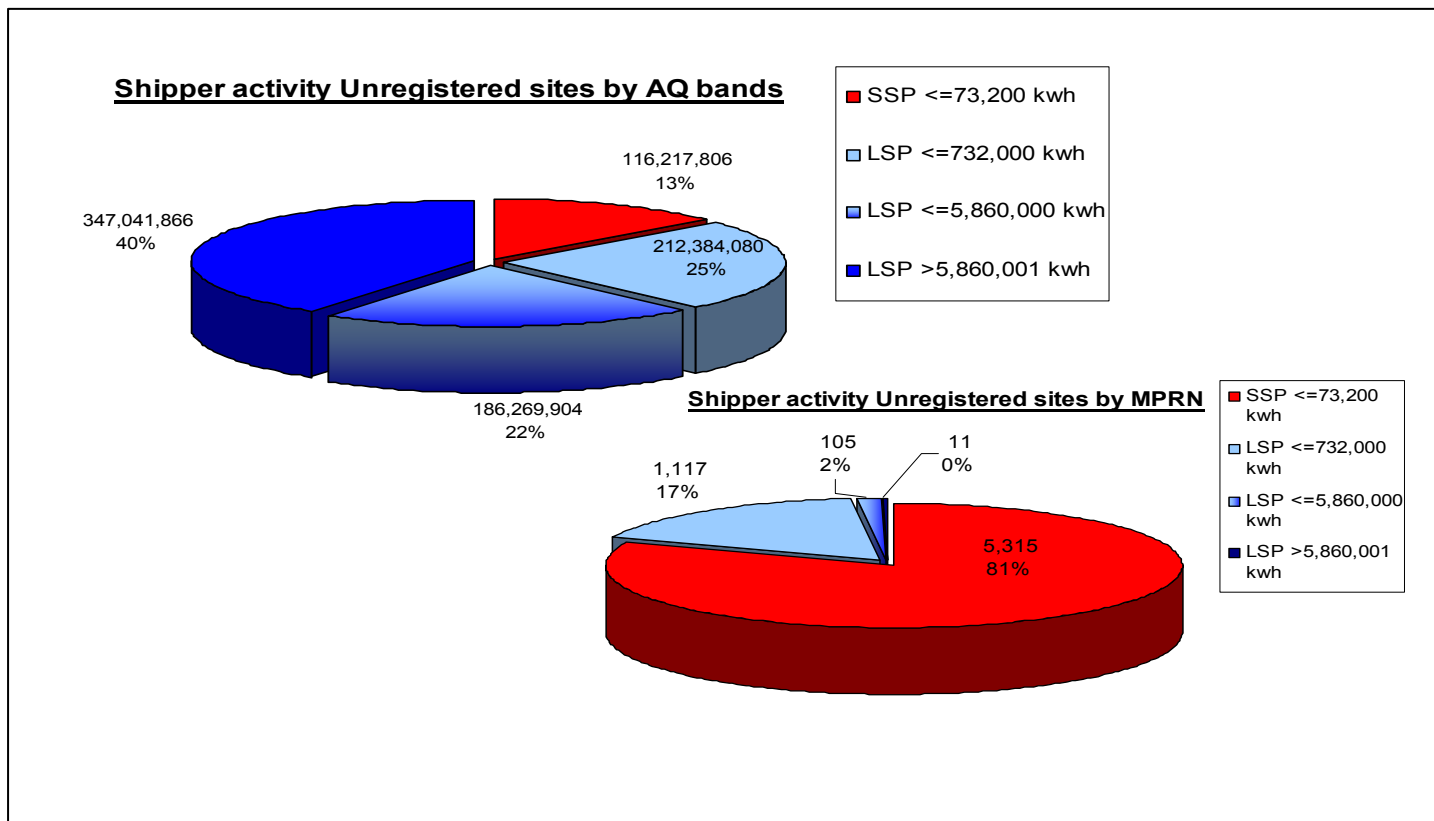
Please contact Chris Warner on 01926 653541 (chris.warner@uk.ngrid.com) should you require any further information with respect to the above.

Yours sincerely

Richard Court
Commercial Manager

Appendix 1

Unregistered Sites where there has been Shipper activity, e.g. attempted RGMA flows, figures as at June 2008.



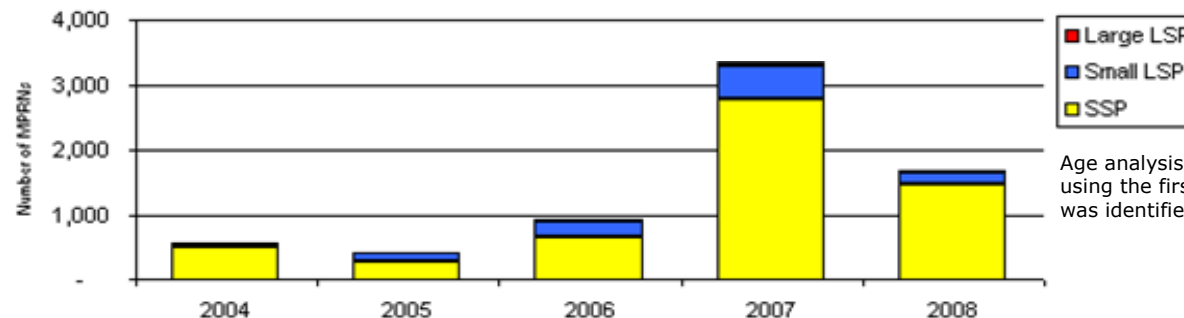
Analysis of Unconfirmed Meter Points with Shipper Activity as at June 2008

To indicate the time taken to confirm an MPRN the following data compares the first date Shipper activity was identified to the current date as it remains unregistered split by load bands.

Date Range	30/06/2004 to 16/06/08	
Total Unregistered Shipper activity MPRNs		6,921
SSP (<=73,200kwh)	81%	5,641
Small LSP (73,201 <=732,000kwh)	17%	1,164
Large LSP (>732,001kwh)	2%	116
Average number of days from activity to date		411
Most recent date		17/04/2008
Oldest date		30/06/2004

NB. It should be noted that this analysis is based on the activity of companies who are requesting MPRN creations and attempting to update the system via C&D and RGMA. There still remains the issue with the majority of unregistered sites where no activity has taken place at all.

Age analysis of Unregistered Shipper activity MPRNs split by load



Age analysis has been calculated using the first date Shipper activity was identified.

Total age analysis of Shipper activity	2004	2005	2006	2007	2008	Total
SSP	500	270	646	2,774	1,451	5,641
Small LSP	72	135	256	510	191	1,164
Large LSP	8	8	26	51	23	116
Total	580	413	928	3,335	1,665	6,921

Total		Total AQ (kwh)	Average days	Oldest date
SSP (<=73,200kwh)	12%	121,366,710	390	30/06/2004
Small LSP (73,201 <=732,000kwh)	21%	213,672,533	505	23/07/2004
Large LSP (>732,001kwh)	67%	673,937,256	446	11/08/2004
Overall total		1,008,976,499	411	

Theft of Gas Allegations Received by xoserve between 01/07/03 and 31/03/08 (Shipper responsibility theft only)

By AQ

Site Type	No of Allegations	%age of Allegations	Valid / Invalid	Reported Stolen kWhs	%age of Total Reported Stolen kWhs	No of Allegations	%age of Allegations
LSP	438	2.6%	Invalid			369	84.25%
			Valid	3913589	3.36%	69	15.75%
SSP	16410	97.4%	Invalid			10748	65.50%
			Valid	112468886	96.64%	5662	34.50%
Totals	16848	100%		116382475	100%	16848	100%

Theft of Gas Contacts Cleared as Valid between 01/07/03 and 31/03/08 with and without kWhs provided (Shipper responsibility theft only)

By AQ

Site Type	kWhs Provided	Number of Contacts	%age of Valid Contacts	Total
LSP	Yes	56	81.16%	69
	No	13	18.84%	
SSP	Yes	937	16.55%	5662
	No	4725	83.45%	
	Total	5731	100%	5731