

Final Modification Report
Framework for correct apportionment of NDM error
Modification Reference Number 0194
Framework for correct apportionment of LSP unidentified gas
Modification Reference Number 0194A
Version 3.0

This Final Modification Report is made pursuant to Rule 9.3.1 of the Modification Rules and follows the format required under Rule 9.4.

1 The Modification Proposal

Proposal 0194

Introduction

Modification Proposal 0194 has been amended following discussion at a UNC Development Workgroup over the last 6 months.

This Proposal seeks to establish a **framework** to facilitate: the identification of causes of RbD error; identifying the extent to which differing market sectors contribute to this error; and the reallocation of this error to the relevant sectors.

This Proposal establishes the framework only and it does not make changes to the present level of reapportionment of RbD error.

The current regime

Energy allocation errors arise because of generic market issues such as LDZ CSEPs creation issues or because of problems within Shippers' control such as the detection of theft and late or unregistered sites. The current RbD allocation places all of the costs arising from energy allocation error solely into the SSP sector. Therefore it does not provide any incentive on Shippers in the LSP market to correct errors that are impacting the SSP market, leading to more costs for SSP suppliers and their customers. The existing arrangements do not target costs correctly, resulting in Shippers with poor performance in the LSP market being protected from any liability.

The energy allocation error has not been caused by SSP meter reading or deeming shortfalls, but is a consequence of measurement failures that are applicable to all non-daily metered sites. These measurement errors include;

- LDZ Off take metering errors
- LDZ shrinkage
- LDZ CSEP reconciliation
- Late registration (Unregistered, unconfirmed and unrecorded sites)
- Supply Point metering errors
- Theft (including unreported meter bypasses)

The current situation fails to provide appropriate incentives to all Shippers to identify and eliminate the source of these errors, such as the detection of theft. Further there is presently no mechanism for reviewing and amending the level of RbD that should be apportioned to different customer groups.

This Proposal

This Proposal is to introduce an “**RbD Allocation Table**” into the UNC, and that the UNC be amended such to require that RbD Energy is allocated in accordance with the percentages indicated in the RbD Allocation Table (the Business Rules included within this Proposal provide further detail of the proposed allocation process). We propose that the new table be an annex to TPD Section E, and the appendix to this Proposal provides a draft of how we believe this table could appear in the UNC, including illustrating the initial row and column headings that we believe are required to give effect to this Proposal.

This Proposal does not seek to change the present levels of contribution made. Hence the proposed RbD Allocation Table should initially include a 100% allocation to the SSP sector, as in the table appended to this Proposal.

We propose that, as in the appendix to this Proposal, the RbD Allocation Table should identify the following contributory factors:

- Read submission issues
- Late Confirmations
- Temperature and pressure correction issues
- LDZ CSEP Reconciliation issues
- LDZ shrinkage errors
- Theft (*which may include unreported open by-pass valves*)
- Supply Point metering
- LDZ metering
- End Supply Metering errors

Similarly, we propose that the RbD Allocation Table should identify the following “**classifications**”;

- SSP (Smaller Supply Points)
- SSP (Remote Meter Reading Equipment)
- LSP NDM (Larger Supply Points Non Daily Metered)
- LSP NDM (Remote Meter Reading Equipment)
- LSP DM (Daily Metered Larger Supply Points – including non-mandatory DM)

We believe that the invoicing solution that would be required to deliver the aims of this Modification Proposal could be achieved by the utilisation of an offline invoicing system. This solution could utilise the current ad-hoc invoicing mechanisms and need not provide a significant impact upon systems, processes or procedures and therefore could be relatively straightforward to implement.

Other Considerations

We have elected to exclude the allocation and charging of transportation costs from this Proposal. This effectively decouples the matter of transportation charging from energy allocation. Whilst there are many commonalities between the way that RbD energy costs and RbD transportation costs can be allocated, the two need not be dependent upon each other, and so can be addressed by separate proposals and at separate times. For the avoidance of doubt, therefore, it is intended that this Proposal only applies to energy charges, and that a separate Proposal would need to be raised to deal with the allocation of transportation

charges. It is also intended that RbD energy charges continue to be allocated at the system average price, consistent with the application of energy charges across all sectors to date. We would stress that this is not to be confused with the matter of transportation capacity and commodity charges for which different rates are applied across different consumption bands and system offtake quantities.

Business Rules

Current RbD processing is unchanged, thus:

1. At M+1 the Aggregate Reconciliation Quantity will be calculated in respect of Month M.
2. At M+1 the Aggregate Reconciliation Quantity and associated charges will be apportioned to Smaller Supply Point (“SSP”) Users in accordance with current UNC provisions.
3. At M+1 Aggregate Reconciliation Transportation Charge Adjustments and any Aggregate Reconciliation Clearing Values (excluded from the new arrangements under point 5) will be issued to SSP Users in accordance with the values established in step 2.

The new arrangements will comprise:

4. Under this proposal the Aggregate Reconciliation Quantity and Aggregate Reconciliation Clearing Value (excluding those items specified in point 5) from Month M will be apportioned to Supply Point (“SP”) Users in accordance with the Apportionment Methodology. The following items are for consideration
 - i. Timing of apportionment - M+1 or M+2 etc (different to transportation invoice timings)
 - ii. Frequency - monthly / 6 monthly / annually etc
 - iii. Variability of the proportion allocated to market sectors (point 6)
5. Non-standard items outside the scope of apportionment under this proposal
 - i. Application of End of Year Reconciliations
 - ii. Application of Large Offtake Metering Adjustment
 - iii. Annual Shrinkage adjustmentwhich will be apportioned in accordance with the prevailing terms
6. The Apportionment Methodology is that the Aggregate Reconciliation Quantity and Aggregate Reconciliation Clearing value determined pursuant to point 4 will be apportioned:
 - a. to SPs within the following sectors in proportion to their SP Annual Quantity (“AQ”) Market Share within each sector

- | | |
|--|-----|
| i. SSP | a % |
| ii. SSP (with Remote Metering Equipment) | b % |
| iii. LSP | c % |
| iv. LSP (With Remote Metering Equipment) | d % |
| v. Daily Meter Sites | e % |

For the avoidance of doubt the sum of values a to e (above) will be 100%.

- b. the AQ market share in (a) will be derived in proportion to their SP AQ Market Share in a consistent manner with existing RbD principles (i.e. excluding sites to which G3.4.3 applies).
 - c. the above percentages may vary from time to time in accordance with the relevant governance rules (proposed to be pursuant to UNC Modification)
 - i. Modification Proposal 0194 advocates the values detailed in 6a as:
 - a. 100%
 - b. 0%
 - c. 0%
 - d. 0%
 - e. 0%
 - d. specific categories of SPs excluded from any application of the Apportionment Methodology and SP Market Shares are:
 - i. NTS Supply Points
 - ii. Special Metering Supply Points (DM)
 - iii. DM CSEPs
7. Aggregate Reconciliation Quantities will be grouped into sectors and apportioned to SP market shares in accordance with the existing RbD sector principles (i.e. in accordance with the 1, 6 and 12 month apportionment rules (E7.2.1/7.2.2(f)).
 8. Reconciliation Invoices will be issued to all Users (SSP and LSP) to reflect net liability (from Month M) as a consequence of the application of the Apportionment Methodology.

Proposal 0194A

Introduction

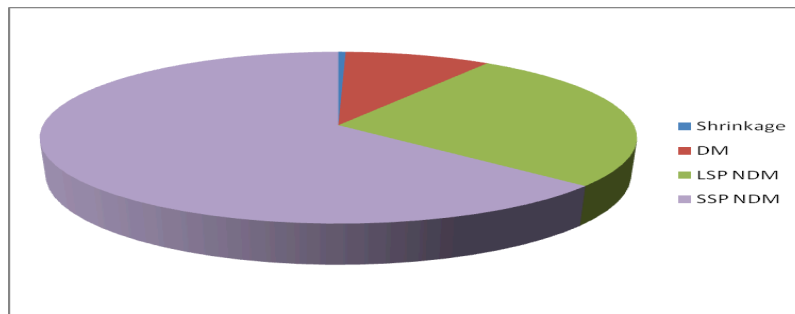
This modification proposal seeks to establish a framework for the identification of causes of unidentified gas, identifying the extent to which differing market sectors contribute to this error, and the allocation of this error to the relevant sectors. For the avoidance of doubt the term “unidentified gas” or energy refers to gas which is supplied to the GB gas network, but whose use cannot be accounted for after all known reconciliations. This is sometimes referred to as unallocated gas or energy. An example of this is gas which is stolen from the network.

The energy allocation regime

The current market arrangements for the GB gas market work on the principle of daily balancing. Only the total amount of gas consumed by the GB as a whole along with the consumption of Daily Metered (DM) sites is known with a reasonable degree of certainty during the initial balancing period. Daily gas consumption for the majority of sites is estimated through a combination of algorithms and site categorisation, based on historical consumption patterns and Annual Quantities.

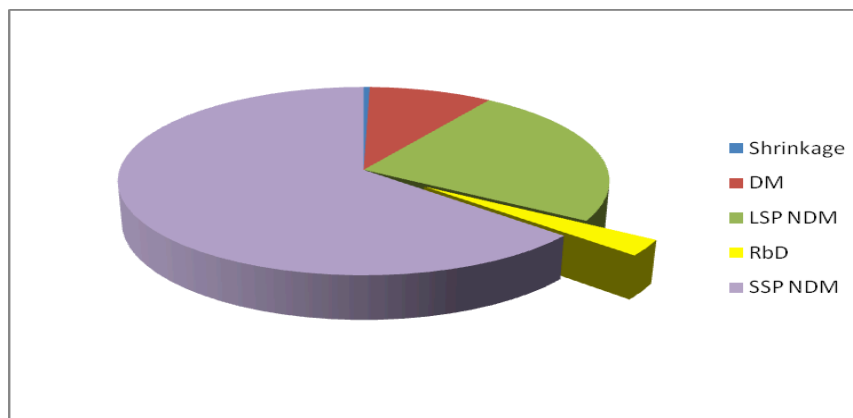
Initially the determination of gas consumption for any given day for Non-daily Metered (NDM) sites is calculated by subtracting DM and transporter losses (Shrinkage) from total GB consumption. This NDM consumption is split between Large Supply Point (LSP) and Small Supply Point (SSP) NDM customers. These sectors are also often referred to as I&C and Domestic respectively.

Initial Allocation of GB Gas Consumption (not to scale)



The initial LSP and SSP NDM consumptions are estimated via behaviour modelling. When a meter reading for a LSP NDM site is obtained, the estimated consumption is corrected and the LSP shipper is credited/debited in accordance with the difference between the estimated and measured consumption. In the case of an underestimation by the transporters of the contribution from the LSP sector, this will create a transfer of energy to the LSP market from the SSP market. Conversely in the case of an overestimation by the transporters of the contribution from the LSP sector, this will create a transfer of energy from the LSP market to the SSP market. This correction volume is termed RbD volume. The underlying principle of RbD is that this re-allocation of gas or energy between the two market sectors occurs irrespective of the amounts involved or the direction of the re-allocation.

Variation of Allocation of GB Gas Consumption through the RbD process. (not to scale)



History of RbD

Subsequent to competition being fully introduced to the Small Supply Point market in 1998, it was decided to allocate the daily changes in the overall Small Supply Point sector by market share, rather than by individual meter point reconciliation. This process, Reconciliation by Difference (RbD), was seen as a cost-efficient mechanism when compared to individual meter point reconciliation. The considerable system costs that would have been incurred by the transporter in developing, maintaining and operating such systems were seen to be unwarranted. Shippers also avoided significant costs through the resolution of issues inherent in an individual meter point reconciliation process.

It was recognised that Small Supply Point consumers are relatively homogenous in both consumption levels and behaviour. This behaviour allowed the development of an aggregate process to adjust allocations in gas consumption. This process was endorsed by the Ofgem review of RbD in 2006¹.

The widely differing nature of gas consumption behaviour of LSP NDM sites justifies the continuation of individual meter point reconciliation for these consumers. In contrast to SSP consumers, LSP NDMs exhibit wide variations in terms of size (annual and peak day), load factor and seasonal consumption habits (such as tourist attractions that open in summer or schools that close during holidays). This distinction is critical when considering extending the impact of the RbD process to market sectors other than SSP.

It is important to note that the current UNC process results in all unidentified energy being assumed to be SSP consumption via the RbD allocation process. Current UNC processes do not allocate unidentified gas to the LSP sector.

How significant the levels of unidentified gas are in each sector is, by definition, difficult to ascertain. The Development Work Group for Modification Proposal 0194 could not uncover any definitive evidence of LSP contributions to the overall RbD error; though a body of anecdotal evidence does exist indicating that some unidentified gas which would properly be allocated to the LSP market is being allocated to the SSP market.

Re-allocation of market error

¹ http://www.ofgem.gov.uk/Licensing/IndCodes/Governance/Documents/1/13487-RbD_FinalV1.1.pdf

Modification Proposals 0115/0115a attempted to allocate some of these measurement errors via RbD. Ofgem gave support to the general principle of spreading the costs of unidentified gas to all market players. In its Modification Proposal 0115 decision letter dated 24th October 2007 Ofgem stated that:

“we agree with the basic tenet of the proposals, that it is inappropriate for one sector of the gas market to bear all the costs of unallocated gas”

The decision letter went on to state that

“there are many issues which are currently contributing to the RbD charge, only some of which have been explored as part of these proposals and not all of these can necessarily be attributed to I&C shippers.”

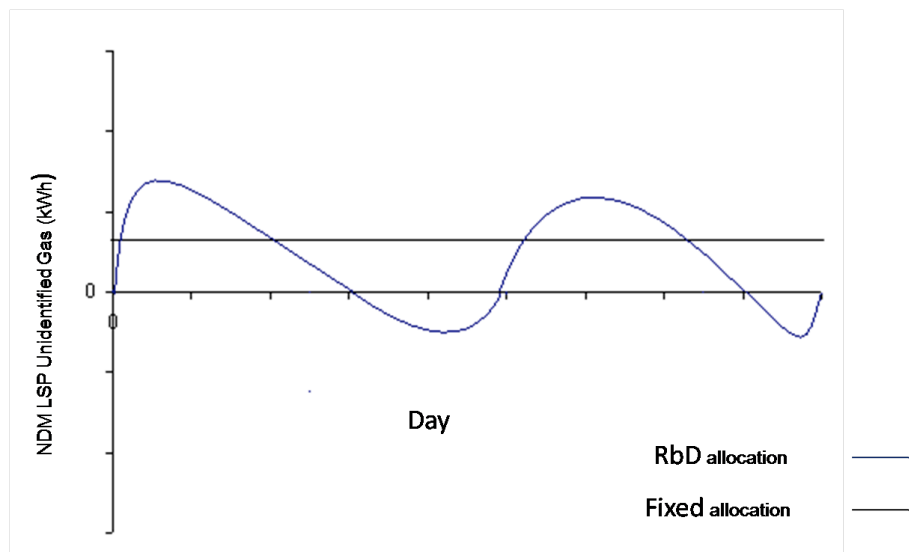
Use of RbD to reflect LSP unidentified gas

The Modification Proposal 0194 Development Work Group has considered the use of RbD to allocate such energy to the LSP market. Significant issues were identified in using this approach, which make it inappropriate. The RbD mechanism improves the initial estimation of gas consumption between SSP and LSP markets by allocating any change in the actual LSP allocation to the SSP sector by market share. At present a percentage of this RbD adjustment includes an element of unidentified gas. However, the majority of such movement between the LSP and SSP market is reflective of actual SSP consumption. The homogeneity of SSPs relative to LSPs makes it appropriate to use the RbD mechanism to allocate this consumption to the SSP market sector.

As the RbD mechanism’s main purpose is to correct initial LSP allocation estimates, with actual data, any extension of this mechanism to the LSP market, as envisaged in Modification Proposal 0194, would almost certainly create a cross-subsidy between the SSP and LSP sectors. Using a proportion of RbD as the estimate of unidentified gas attributable to the LSP sector would also inappropriately assume that the unidentified gas error varies as RbD varies. This would be illogical. Furthermore, in the event of a credit of additional energy to the LSP market, the LSP sector would receive a financial credit for the level of unidentified gas in its sector through RbD. Again, this would be illogical.

Comparison between use of RbD and a fixed allocation method to determine unidentified LSP gas(not to scale)

² <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=362&refer=Networks/GasDistr/GDPCR7-13>



The Modification Proposal 0194 Development Work Group also considered the way in which transporters take into account theft and leakage as part of their network responsibilities. These losses (shrinkage) are currently estimated as discrete values based on analysis of network operations. In moving from a sliding percentage of total throughput to fixed volumes, Ofgem noted as part of its GDPCR consultation “*The evidence available shows that there is little correlation between shrinkage and throughput for the existing networks²*”. A fixed value was considered more appropriate.

We agree with Ofgem’s analysis and so propose that a methodology aimed at fairly and accurately allocating a volume of gas to the LSP NDM Sector should be based on that used for Shrinkage allocation.

Identification of Error

We believe that for these purposes the LSP market can be divided into two sectors, namely:

- NDM (Non Daily Metered)
- DM (Daily Metered – including Non-Mandatory DM)

While we have considered the use of sites equipped with AMR (Automated Meter Reading) as a separate category, it has been indicated by xoserve that the identification of NDM AMR sites would be very difficult as such sites are not explicitly identified within their systems at present. In the event of sizeable take-up of advanced metering in the market, then the methodology may be easily modified to reflect this.

The methodology will identify differing market activities that are contributing towards to the overall market error, namely:

- **Late confirmation, unregistered and orphaned sites.** It is our view that late confirmation LSP sites contribute nugatory levels of unidentified gas, as sites which are confirmed at some stage will have their estimated consumption

corrected. We recognise that, in rare cases, late confirmation may occur where all of the energy may not be reconciled after the four year cut-off date. For Unregistered and orphaned sites, however, it is appropriate for the LSP sector to be allocated a suitable proportion.

- **Late Confirmation, unregistered and orphaned IGT.** We recognise that due to the greater propensity to new connections within IGT networks it is likely that these sites pose a more significant issue compared to DN sites and hence a separate value is appropriate.
- **NDM Shrinkage contribution.** Such shrinkage losses that are not accounted for by the transporters allowance. As DM sites are Daily Read and therefore don't use an estimation process such difference between the transporter allowance and the shrinkage losses should be confined to the NDM sector.
- **Theft and Unreported open meter by-pass valves.** The large majority of theft both alleged and proven is in the domestic sector. We do recognise that in the rare instance of theft at an LSP site, the volume of gas stolen per site tends to be greater than that at a SSP site and so consideration should be given to the level of such theft.

Outside of the late confirmation, unregistered and orphaned IGT charge, we have not made a distinction between IGT and DN sites, as we believe the issues that we have identified apply to all networks and there is no direct evidence that differentiation will enhance efficiency. In some cases, it is our view that this equal treatment is a benefit for the SSP market. For example, we believe that the majority of unregistered sites on IGT networks are SSPs.

It is envisaged that the values of these contributions to unallocated gas volumes should only be amended annually, using the same timetable as for the main announcement of LDZ transportation charges for the forthcoming year, as envisaged in the GT Licence which provides for a single annual change to these charges. This is to ensure that Shippers are able to include the impact of the envisaged allocation process as well as any change in transportation charges in their charges to their end-users. We would anticipate that the process for establishing the volume of gas to be allocated to the LSP sector would be similar to that for the transporters shrinkage calculations. For the LSP (NDM and DM) market sectors, these annualised volumes would then be apportioned monthly on the basis of total market share, measured by volume. It is not appropriate to apportion costs by site, as the profile and consumption of LSP sites vary significantly. The prices to determine the final charge will be based on 30 day rolling SAP for the relevant month.

For the SSP market, the contribution of unidentified gas will be maintained as part of RbD. This mechanism remains a valid method of apportioning unallocated energy as SSP sites are relatively homogenous in consumption and behaviour.

By reducing the amount of gas accruing to RbD, the money accumulated from the LSP market would effectively be credited to SSP Users on the same proportional basis as RbD.

This Modification Proposal itself does not seek to determine the precise levels of unidentified gas that might properly be allocated to the LSP market. It is the Proposer’s intent that independent industry analysis populates the matrix with values thus informing a revised and fairer apportionment of costs to various market sectors.

Our proposal

1. It is proposed that the UNC be modified to include provisions which provide for the allocation to the LSP sector of specific volumes of otherwise unidentified gas. We envisage that this could be achieved by adding an appendix to Section E, the “Large Supply Point unidentified gas allocation table”, and cross referencing this Table as appropriate within the UNC. This table could then be used to allocate unidentified gas (which would otherwise fall to RbD) attributed to individual causes to the LSP sector. The initial table will show zero volumes allocated to the LSP sector, thereby maintaining the status quo but facilitating population of the table through implementation of further Modification Proposals.

It is envisaged that the table could be introduced in the following format:

Source of error (AQ)	Market Segment	
	LSP NDM (kWh)	LSP DM (kWh)
Late confirmation, unregistered and orphaned Sites	0	0
Late Confirmation, unregistered and orphaned Sites (IGT)	0	0
Shrinkage contribution	0	0
Theft and Unreported open meter by-pass valves	0	0

These causes are collectively referred to below as “NDM LSP unidentified gas”. NB. For the avoidance of doubt please note that this Proposal limits itself to the consideration of energy charges and Transportation charges are excluded.

2. Any change to the size of each contribution of the NDM LSP unidentified gas, i.e. variation in the values in the table, shall be introduced through the implementation of a Modification Proposal. It is envisaged, but not considered to require any explicit UNC reference, that any proposal to vary the values in the table should be implemented in line with the same notice period and start date as for LDZ transportation charges, as specified in GT Licences.

3. AT M+1, the monthly NDM LSP Error Charge will be calculated for the relevant calendar month (“M”).
4. The calculation of the monthly NDM LSP unidentified gas cost shall be 1/12 of the overall NDM LSP unidentified gas (as specified in the proposed table) multiplied by the rolling average 30 day SAP starting on the 1st calendar day of month M.
5. At M+1 the NDM LSP unidentified gas costs will be levied on users as a proportion of their NDM LSP market share in month M. This market share will be derived from the site AQs in the shipper’s ownership. For the avoidance of doubt this will include LSP AQs for sites situated on LDZ CSEPs within the relevant shipper’s ownership. The transporters will raise debit invoices to all Shippers for their proportion of the unidentified gas. It is not envisaged that there will be any specific query process however standard invoice query rules would apply.
6. Provisions will be made for a reduction in RbD of the same value as the proposed debit invoices to the LSP sector. The reallocation of the accrued NSM LSP unidentified gas costs payments to the SSP Shippers will be made on the basis of their NDM SSP market share. Following feedback from xoserve it has been decided that this will be done following current RbD rules. It is therefore proposed that all refunds go into the one month RbD pot for calculating market share.

Comparisons with Modification Proposal 0194

Similar to Modification Proposal 0194 this Proposal limits itself to the reallocation of energy charges, such that Transportation charges are excluded.

A key concern with Modification Proposal 0194 is the linking of the SSP and LSP segments through the proposed extension of RbD. It would be difficult for LSP Shippers to contract in a way which mitigated the consequent risk of RbD exposure since its daily variance does not relate to the activities of the customer base.

It is the opinion of the Proposer and a number of members of the 0194 Development Work Group that there is no positive correlation between the size of the RbD energy allocation and the energy which should be applied to individual error categories. For example, it is wholly untenable that as the RbD volume varies there is a proportionate variation in the volume of Late Confirmed sites. As it is conceivable that RbD can provide a net credit to the LSP community, the use of RbD may also create the perverse outcome that LSP shippers are compensated for unidentified gas

This is further complicated by the fact that the sample data acquired by xoserve through the RbD Verification Process suggests that the level of the RbD “Remaining Balance” is not significant. In fact it is within the 95% Confidence Level established through the Normal Distribution Sample Testing technique.

We believe that a methodology analogous to that developed by Ofgem for the current DN shrinkage process is simpler, cheaper and easier to apply than that put forward in Modification Proposal 0194, and better achieves the aims of the fair apportionment of unidentified gas. This alternate Modification Proposal does not extend RbD to the LSP market. The basis for this Modification Proposal is to allocate a fixed volume to the LSP

sector for each of the error categories which best reflects the LSP Sector contribution to the error. This removes the anomaly proposed in Modification Proposal 0194 that error volumes move in parallel with RbD volumes.

2 **Extent to which implementation of the proposed modification would better facilitate the relevant objectives**

Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;

British Gas considers implementation of Proposal 0194 would enable the more efficient operation of the pipeline system as follows;

- i) Any reduction in theft will reduce the volume of gas unnecessarily transported and the associated safety risks and costs that come with it. These could extend to pressure management issues.
- ii) Improved data management including operation of registration processes, management of IGT data etc shall in turn give greater confidence in system planning, demand forecasts and so on.

Total considers implementation of Proposal 0194 would lead to arbitrary cost allocation to the LSP sector, leading to potential cross-subsidies of the SSP market. It will therefore not incentivise good practice and will not reduce any of the root causes relating to unallocated gas and hence would not further this relevant objective.

Total considers that implementation of Proposal 0194a would provide predictable and definite cost allocation. This would encourage good practice by Shippers who will have the certainty that reductions in unallocated gas in the LSP market sector will positively impact their business. This can be expected to improve the efficiency of the pipeline as losses are reduced, hence furthering achievement of this relevant objective.

Standard Special Condition A11.1 (b): so far as is consistent with sub-paragraph (a), the 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;***

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (c): so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;

EDF Energy notes that Standard Licence Condition 4D requires all of the GTs to not discriminate between market participants. The LSP Sector contributes to the volumes of unallocated energy; however all of the costs for unallocated energy are borne by the SSP Sector. Implementation of either proposal would provide a framework which would help to ensure costs are correctly targeted and so help to facilitate Standard Licence Condition 4D.

EDF Energy however notes that by choosing a flat profile for the allocation of energy to the LSP sector, there is a possibility that a cross subsidy from the SSP to LSP sector would remain. In particular EDF would note that the GDPCR appeared to recognise that theft varies with throughput and so follows a seasonal profile. There is therefore a risk that the LSP

sector will be over allocated unaccounted for gas in the summer, when prices are lower, but under allocated gas in the winter when prices are historically higher. This would appear to continue with the cross subsidy, although at significantly reduced levels from what is currently present.

Shell Gas Direct believes that 0194A, unlike 0194, would not discriminate between market participants - in this case, market participants who supply domestic and I&C customers, as opposed to those who supply only the latter.

Standard Special Condition A11.1 (d): so far as is consistent with sub-paragraphs (a) to (c) the 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 Proposals provide a framework which would make it easier for Shippers to propose different allocations, thereby potentially facilitating competition.

However, making it easier to propose different allocations increases risk and uncertainty thereby adversely impacting competition. By introducing a framework based on allocating RBD Energy percentage shares, some DWG Members felt that, in the case of 0194, there would not be an accurate allocation between Shippers were there to be any move away from the present approach, creating perverse incentives that would adversely impact competition.

EDF considers a driving force behind a competitive market is to ensure that costs are targeted at those who are causing them. Implementation of either Proposals would make it easier for Shippers to propose different allocation of costs, and so help to ensure that costs are correctly targeted, thereby facilitating competition. In addition, implementation may increase the risk that the LSP sector has to fund the gas that it is consuming, this will conversely reduce the risk for SSP suppliers that they will have to fund gas consumed in the LSP market - re-attributing risk to the appropriate market sectors could also be viewed as being beneficial to competition.

Scottish Power considers implementation of Proposal 0194 would introduce a much-improved basis for the equitable allocation of RbD costs across all market sectors and, as a consequence, suggest that competition between Shippers would be improved with the re-balancing of risk exposure. This in turn should give greater confidence and assurance to new entrants who may be proposing to enter and operate primarily within the SSP market sector.

Total considers implementation of Proposal 0194 would be detrimental to competition in the LSP sector as it would allocate a fluctuating level of gas to the LSP market that bears no relation to the size of root cause. In addition Proposal 0194 is detrimental to competition as it would squeeze those Suppliers purely in the I&C market, whereas for those Suppliers in both the LSP and SSP markets, any cost will be offset by a benefit.

Total considers implementation of Proposal 0194A would result in a better and more stable allocation of costs, hence ensuring competition as Shippers will be able to have a degree of control over future costs incurred. As Shippers can better manage the allocation risk, the price impact on LSP customers would be ameliorated.

Standard Special Condition A11.1 (e): so far as is consistent with sub-paragraphs (a) to (d), the 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;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (f): so far as is consistent with sub-paragraphs (a) to

(e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;

The Proposals provide a framework which would make it easier for Shippers to propose different allocations; thereby potentially promoting efficiency in the administration of the UNC should subsequent Modification Proposals be raised. However, if no such Proposals are raised implementation of either Proposal would be superfluous and hence implementation would not promote efficient administration of the UNC.

3 The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation

No implications on security of supply, operation of the Total System or industry fragmentation have been identified.

4 The implications for Transporters and each Transporter of implementing the Modification Proposal, including:

a) Implications for operation of the System:

No implications for operation of the System have been identified.

b) Development and capital cost and operating cost implications:

No development or capital costs have been identified as a result of implementing the proposed frameworks which retain the existing allocation rules.

c) Extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs:

Not applicable.

d) Analysis of the consequences (if any) this proposal would have on price regulation:

No consequence for price regulation has been identified.

5 The consequence of implementing the Modification Proposal on the level of contractual risk of each Transporter under the Code as modified by the Modification Proposal

No such consequence is anticipated.

6 The high level indication of the areas of the UK Link System likely to be affected, together with the development implications and other implications for the UK Link Systems and related computer systems of each Transporter and Users

No changes to systems would be required as a result of implementation of either Proposal.

7 The implications of implementing the Modification Proposal for Users, including administrative and operational costs and level of contractual risk

Administrative and operational implications (including impact upon manual processes and procedures)

No such implications have been identified.

Development and capital cost and operating cost implications

No such costs have been identified.

Consequence for the level of contractual risk of Users

By making change easier, introducing either proposed framework would increase contractual risk for LSP Shippers in particular, and change the nature of LSP risk as a result of exposure to RBD, while reducing risk for SSP Shippers.

While noting that the degree of re-attribution varies between the Proposals, EDF Energy considers that implementation of either Proposal would help to ensure that risk is re-attributed to the appropriate market sectors. EDF Energy considers that whilst implementation of Proposal 0194A would reduce risk to SSP Shippers and increase it to LSP Shippers, this will be offset by the introduction of a flat profile for unallocated energy to LSP Shippers. In the GDPCR Ofgem appears to recognise that theft varies with throughput. There is therefore a risk that unallocated energy is misallocated between market sectors throughout the year. Given the existence of a summer/winter spread in prices, EDF Energy considers that, relative to Proposal 0194, this would increase risk to SSP Shippers and decrease risk to LSP Shippers.

Total considers that implementation of either Proposal would increase contractual risk to the LSP sector, though the level of risk is significantly higher with 0194.

8 The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non Code Party

I&C consumers may be impacted to the extent that I&C contracts are modified to reflect the existence of the framework within the UNC.

Total considers that while implementation of either Proposal would assign additional gas to LSPs, resulting in additional costs, Proposal 0194 would assign significant, varying levels of gas to LSPs, potentially resulting in large and unpredictable costs whereas Proposal 0194a would create additional costs to LSPs in a predictable and equitable fashion.

9 Consequences on the legislative and regulatory obligations and contractual relationships of each Transporter and each User and Non Code Party of implementing the Modification Proposal

Total notes there is no facility within its IT systems to bill out any additional costs associated with implementation of either Proposal, and no contractual clauses in place to do so.

10 Analysis of any advantages or disadvantages of implementation of the Modification Proposal

The 0194 Development Work Group was polarised and neither the advantages nor disadvantages of Proposal 0194 were accepted by all.

Advantages

Advantages identified by some were:

- Provides a framework which simplifies subsequent change to the allocation of RBD Energy
- The Proposal uses the existing RBD mechanism, with which SSP Shippers are familiar.

EDF Energy considers the advantages of implementing 0194 are:

- Re-attributes risk to the appropriate market sector.
- Uses the RbD mechanism with which the majority of Shippers are familiar with. However no evidence has been provided to demonstrate whether it is appropriate or not.
- Facilitates Gas Transporter Standard Licence Condition 4D.

Disadvantages

Disadvantages identified by some were:

- The Proposal uses the existing RBD smear as the basis for reallocation. The issues highlighted in the table are not directly proportional to the RBD smear, which through the percentage mechanism is the basis on which this modification is proposed.
- The Proposal introduces the concept of allocation by percentage market share, which does not reflect the diversity of the I&C market.

Total is concerned Proposal 0194 uses the existing RBD Volume as the basis for reallocation of unidentified gas, but this volume has no relationship with the root causes identified. Allocation using this model would lead to misallocation between the LSP and SSP markets.

Proposal 0194A

The Proposer identified the following:

Advantages

As this proposal seeks to provide a framework for the determination of unidentified gas values that the market must account for, neither itself nor Modification Proposal 0194 creates any immediate changes in gas allocation. It does have the following benefits however:

- This Proposal creates a clear and simple framework to allow consideration of the levels of unallocated gas to be allocated between LSP Shippers.
- The framework retains a level playing field between all shippers whether LSP NDM, LSP DM or SSP by ensuring there are no unintended cross

subsidies.

- This Proposal provides a framework which can more accurately target costs at the LSP NDM sector, unlike Modification Proposal 0194 which assumes a linkage between RbD volumes and contributions to unidentified gas.
- This alternate Proposal avoids much of the complexity that is proposed by Modification Proposal 0194 and allows a greater range of solutions to be considered when determining appropriate values of unallocated gas to be apportioned to the LSP market.
- This Proposal maintains the separation between the LSP and SSP NDM markets, something which Modification Proposal 0194 would erode.

EDF Energy considers the advantages of implementing 0194A are:

- Does not utilise the RbD mechanism, which may appear attractive to some LSP Shippers. However no evidence has been provided to demonstrate whether this is appropriate or not.
- Re-attributes risks to the appropriate market sector, although not to the same degree as 0194.
- Facilitates Gas Transporter Standard Licence Condition 4D.

Total considers 0194A would establish a link between costs and root causes. Implementation would create a clear and simple framework to allow consideration of the levels of unallocated gas to be allocated to LSP sites and reduce the probability of cross-subsidy between market sectors. The allocation process is also easy to administer and allows Shippers with LSP portfolios to procure additional gas to cover these losses without incurring excessive costs.

Disadvantages

EDF Energy considers 0194A has the following Disadvantages:

- Uses a flat profile for the allocation of unaccounted for gas to the LSP market - this appears to be in contradiction to Ofgem's views in the GDPCR on theft profiles.
- The use of a flat profile potentially creates a cross subsidy from SSP to LSP Shippers.
- Different treatment of shrinkage errors to the DM market, compared to the shrinkage regime.

Total considers that, whilst significantly better than Proposal 0194, implementation of 0194A would still provide risk to the LSP Sector as there is still a price factor that would provide some level of uncertainty and there is currently no mechanism in place to pass this on to the end user.

11 Summary of representations received (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)

ORGANISATION	PROPOSAL		PREFERENCE
	0194	0194A	
British Gas	Support	Not in Support	0194
Corona Energy	Not in Support	Support	0194A
EDF Energy	Support	Support	Marginal Preference for 0194
E.ON UK		Support	0194A
Gaz de France	Not in Support	Support	0194A
Gazprom	Not in Support	Support	0194A
Major Energy Users	Not in Support		N/A
National Grid	Qualified	Qualified	Preference for 0194A
Distribution	Support	Support	
Northern Gas Networks		Qualified	0194A
RWE Npower	Qualified	Qualified	Marginal Preference for 0194A
Scotia Gas Networks	Not in Support	Not in Support	N/A
Scottish and Southern	Support	Not in Support	0194
Scottish Power	Support	Not in Support	0194
Shell Gas Direct	Not in Support	Support	0194A
Statoil	Not in Support	Support	0194A
Total	Not in Support	Support	0194A

British Gas provided additional information and evidence within its representations, including a report by Cambridge Economic Policy Associates, in support of Modification Proposal 0194. British Gas considers proposal 0194A seeks to leave any risk associated with the variability of RbD with the domestic sector.

National Grid Distribution provided additional supporting information within their representation for 0194 and 0194A.

A number of representations raised issues concerning the impact of implementing Proposal 0194 on the LSP market and the potential impact on competition in this sector as LSP Shippers would not be able justify passing on additional RbD costs to their customers, severely impacting their business models.

Corona believes it is essential that, if Ofgem is minded to implement Proposal 0194, that they first conduct a Regulatory Impact Assessment. This should help ensure that the full impacts of any decision including the destructive affect it will have on competition are completely understood prior to a decision being made by the Authority.

EDF Energy questions Proposal 0194A's treatment of shrinkage error costs that are not accounted for by the Transporters' allowance - the proposal to only recover any error in shrinkage costs from the NDM market appears inconsistent with current practice.

A number of representations were concerned that 0194 and 0194A should not be considered separately but should be considered in conjunction with other Proposals raised to identify the apportionment and allocation of energy associated with RbD.

Gaz de France considers 0194 does not meet the relevant objectives as many Industrial and Commercial only Shippers do not currently receive RbD invoices as all their portfolio is reconciled on a meter point by meter point basis. These Shippers face the costs of the individual meter point reconciliation regime, plus added costs from RbD, without the significant benefits associated with RbD gained by the SSP sector.

Within its representation, Scottish Power concluded for the re-apportionment of costs, we support the principle that this should be directly related to the volume of the RbD error and not on a pre-determined fixed value as proposed under Modification 0194A. Currently, the SSP market sector is exposed to undue levels of risk exposure as a consequence of energy allocations that they have not wholly contributed to. It is wrong to persist in the discrimination of this one market sector in order to continue the stability of another.

Total concluded that there is no direct correlation between the RbD volume and the root causes of unallocated gas. Month on month the RbD volume varies considerably, pushing volume between the sectors in both directions.

12 The extent to which the implementation is required to enable each Transporter to facilitate compliance with safety or other legislation

Implementation is not required to enable each Transporter to facilitate compliance with safety or other legislation.

13 The extent to which the implementation is required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence

Implementation is not required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence.

14 Programme for works required as a consequence of implementing the Modification Proposal

No programme for works has been identified.

15 Proposed implementation timetable (including timetable for any necessary information systems changes and detailing any potentially retrospective impacts)

Implementation could be immediate on receipt of a decision.

16 Implications of implementing this Modification Proposal upon existing Code Standards of Service

No implications of implementing this Modification Proposal upon existing Code Standards of Service have been identified.

17 Recommendation regarding implementation of this Modification Proposal and the number of votes of the Modification Panel

At the Modification Panel meeting held on 20 November 2008, of the eight Voting Members

present, capable of casting ten votes, three votes were cast in favour of implementing Modification Proposal 0194. Therefore the Panel did not recommend implementation of this Proposal. At the same meeting, seven votes were cast in favour of implementing Alternative Proposal 0194A. Therefore the Panel recommended implementation of Alternative Proposal 0194A.

The Panel then proceeded to vote on which of the two Proposals would be expected to better facilitate achievement of the Relevant Objectives. Of the eight Voting Members present, capable of casting ten votes, one vote was cast in favour of implementing Proposal 0194 in preference to Alternative Proposal 0194A, and eight votes were cast in favour of implementing the Alternative Proposal 0194A in preference to Proposal 0194. Therefore, the Panel determined that, of the two Proposals, Proposal 0194A would better facilitate the achievement of the Relevant Objectives.

18 Transporter's Proposal

This Modification Report contains the Transporter's proposal to modify the Code and the Transporter now seeks direction from the Gas and Electricity Markets Authority in accordance with this report.

19 Text

Legal text for Proposals 0194 and 0194A have been published as separate documents.

For and on behalf of the Relevant Gas Transporters:

Tim Davis
Chief Executive, Joint Office of Gas Transporters