John Bradley
UNC Modifications Secretary
51 Homer Road
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06 February 2009

Dear John,

Response to UNC Modification Proposals 228,228A

Thanks you for the opportunity to respond to the above modification proposals. GDF Suez Energy UK does not support the implementation of either of these proposals.

During discussions on previous related modification proposals UNC 0115 and 0115a, which were subsequently rejected by the authority, it was widely accepted that there should be a mechanism developed to apportion some elements of unallocated gas costs which are currently bourn solely by RbD participants to the Industrial and Commercial sector. UNC 0228 and 0228a both seek to implement different models identified in UNC 0194 and 0194a, via an allocation table in the UNC, to allow unallocated gas costs to be apportioned more widely. Further to UNC 0194 and UNC 0194a these proposals suggest the proportion of energy to be apportioned via this table.

It is important to recognise that a further modification proposal has been raised in this area (UNC 0229) and GDF Suez Energy UK considers that the whole suite of proposals should be considered by Ofgem on their relative merits before any implementation decision is made in this area. Also, given the magnitude of costs under consideration it is essential that a Regulatory Impact Assessment is undertaken to assimilate the relative benefit of each change proposal.

UNC 0228

The model proposed by British Gas under UNC 0228 seeks to apportion a level of cost to the Large Supply Point (LSP) sector based on the monthly volumes billed via Reconciliation by Difference (RbD).

The table below shows the level of RbD volumes which have been billed to the Small Supply Point market over the previous 18 months.

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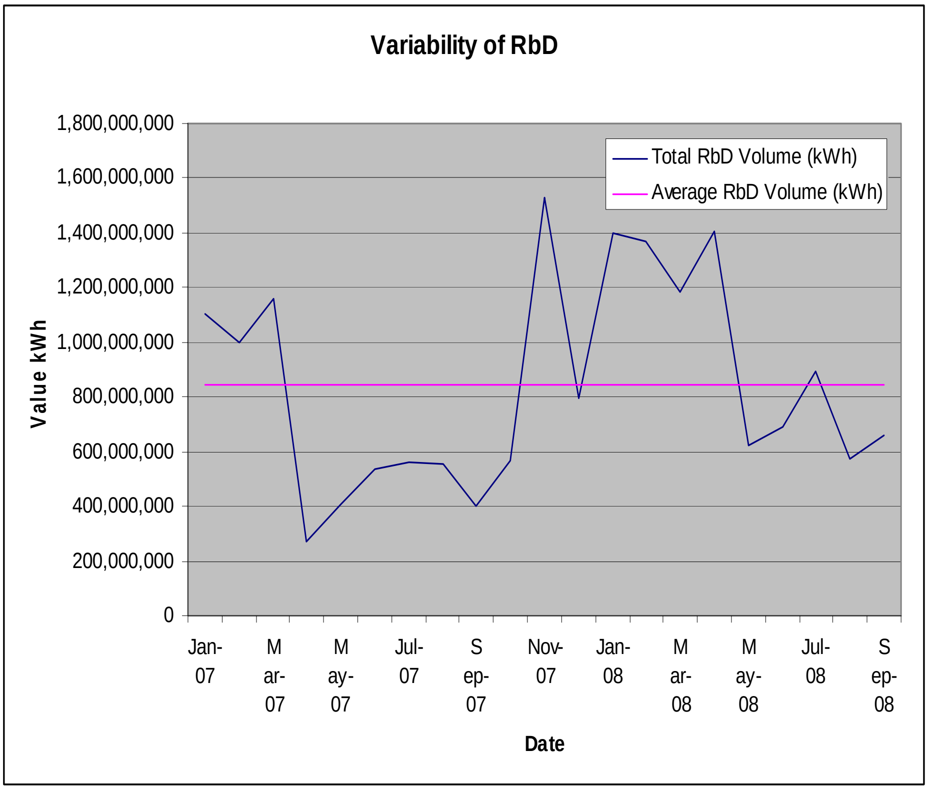
Chart 1 – Variability of RbD



As can be seen from the table, the level of RbD is variable and unpredictable. Volumes have been seen to vary from the mean of around 800GWh frequently and significantly. In December 2007 the variance was close to 100% at a value of nearly 1,600GWh. This is entirely to be expected from a mechanism whose primary objective is to reconcile errors in initial allocation. Such a mechanism can be expected to produce such erratic results as illustrated above.

Over time RbD has developed to perform a secondary function which is effectively to allocate the costs of certain types of pollution. These items of pollution are the areas which have been identified as elements in the allocation table and include unidentified theft of gas and late registrations. It is clear that such items are not variable or erratic in nature when viewed from an industry perspective. Volumes and costs arising from such pollution are generally constant in their both their overall presence and nature.

UNC proposal 0228 is flawed there in its approach. By allocating volumes and costs via a portion of the monthly RbD pot, it introduces unnecessary volatility and risk to LSP shippers instead of a fair and reflective representation of any pollution caused by this sector.

Further to the structural changes identified above and were also contained in its previous 0194 proposal, this modification introduces a volume allocation to Large Supply Points (LSPs). This methodology is severely flawed in the way that costs are attributed to theft where this is not backed by evidence. The sector of theft as proposed is misleading in its name and more so in relation to its content. This sector is in actuality a balancing factor which makes up 76% of the cost re-allocation very little of which is comprised of theft itself or even perceived theft. It is clear that there is further work required by independent analysis to improve the accuracy in this area, otherwise disproportionate costs could be bourn by the LSP sector and introducing a substantial cross-subsidy.

UNC 0228a

UNC 0228a proposes that any identified costs appropriate to the LSP sector are allocated on a fixed annual volume basis as proposed under UNC 0194a. It is unfortunate that 0228a was submitted on the last permissible day without any opportunity for discussion at workstream. The modification offers no new thinking on the issue of volume allocation, and particularly “theft”, between SSP and LSP sectors over and above that proposed by 0228 original.

Relevant Objectives

Both UNC 0228 and 0228a deal only with apportioning costs between SSP and LSP shippers and as such the only relevant objective to address under this proposal is A11.1 d “securing effective competition between relevant shippers and suppliers”.

As stated above, 0228 introduces unnecessary volatility and risk to LSP shippers via an inappropriate method. This allocation method disproportionately damages competition between sectors. Shippers who are active in both the SSP and LSP sectors will benefit unfairly from this change as a cross-subsidy will be introduced.

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.

UNC 0228 will act as a barrier to new entry and discourage participation in the LSP sector as it adds complexity and risk.

Whilst UNC 0228a proposals a more acceptable framework compared to the original it introduces the same costs on the LSP sector which distorts competition to the same extent.

I trust this information is helpful and if you have any questions or would like to discuss further, please do not hesitate to contact me on 0113 306 2104 or mobile 07733 322460.

Yours Sincerely,

P.Broom

Phil Broom
Regulatory Affairs Manager
GDF Suez Energy UK