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Mr Bob Fletcher,
Joint Office of Gas Transporters
51 Homer Road
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8th January 2008

Dear Bob,

RE: MODIFICATION PROPOSAL 228A – Correct Apportionment of NDM Energy

British Gas fully supports the implementation of both our Modification Proposal 228 and Scottish Power's Modification Proposal 228A. However, we have a preference for our own proposal 228 as we believe that this would create a much stronger incentive regime.

Please note, we have submitted a separate response in relation to the original proposal 228.

We welcome many aspects of Scottish Power's proposal, which shares significant similarities to our own proposal 228. Significantly, Scottish Power's alternate proposal uses the same source data and makes the same interpretations and levels of allocations as our original. This alternate proposal is based upon the same framework mechanism as that contained in Modification 194A, proposed by Corona Energy. As a result, unlike the original proposal, it does not link the correction of errors that manifest in RbD to the actual RbD volume during the month.

Whilst we are supportive of Scottish Power's proposal, because it makes a significant step towards mitigating some of the risk borne by the SSP market, we believe that Modification 228 better facilitates the relevant objectives because it maintains the link between errors which manifest in RbD charges and the actual RbD volumes, which strengthens the incentives it is aiming to introduce.

It is our view that Modification Proposal 228A would not create as robust an incentive regime as the original proposal, due to it's lack of responsiveness to changes in behaviour and the increased likelihood of these costs being passed directly through to customers;

Responsiveness to change

Under Modification Proposal 228 the costs of RbD are passed through month on month to suppliers and so as the causes of RbD are tackled by changes in behaviour an immediate benefit will flow through RbD. Whereas in 228A the costs are fixed and so do not immediately respond to changes in behaviour that they are incentivising. Rather these will only be reflected once the charge values are updated annually.

This could lead to an inequitable situation whereby Shippers in the LSP sector make significant process improvements that reduce the level of RbD at the beginning of a Gas Year, but must then wait until the following year before the new level of charge is created and the see benefits from their changed behaviours.

Likelihood of pass through to consumers

Modification Proposal 228A would create a regime where the costs associated with RbD error are fixed at the beginning of a period and do not vary. It is more likely that these costs would then be passed directly through to consumers either through increased tarriff pricing or as a direct pass through charge. This would result in the Shipper becoming 'cash neutral' to the process and so mitigate the incentive.

Our proposal 228 would base the allocation of costs upon the actual RbD volume and so would be directly driven by Shipper actions and so will be to some extent variable and so is less likely to be passed directly through to consumers.

Therefore, overall we believe that 228 will place far stronger incentives on suppliers and greater overall benefits to consumers.

How this proposal better facilitates the relevant objectives

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

This proposal provides a framework and methodology which would result in a more precise and efficient mechanism than the current arrangements for the determination of the apportionment of RbD costs to Shippers.

Although by setting fixed values rather than relating the issues to RbD throughput the incentives this proposal does not create the most responsive incentive regime, it does provide an incentive for LSP shippers to take actions to address some of the issues contributing to RbD.

Therefore, as a result of this proposal the extent to which measurement failures, and especially Theft, persist would be reduced. A reduction in the volume of energy transported through the system and then “lost” will improve efficiency. Improved confidence in throughput data through the reduction in error will also help improve the efficient and economic operation of the pipeline system.

A11.1 (d) – the securing of effective competition (i) between relevant shippers and (ii) between relevant suppliers.

This proposal would reduce the extent to which the predominantly domestic Small Supply Point Market sector, and Shippers / Suppliers operating within it, cross subsidise Shippers / Suppliers operating in the Large Supply Point Market. The reduction of a cross subsidy between market sectors and individual Shippers / Suppliers operating in them, better secures effective competition between Shippers and Suppliers.

Under the current arrangements, Shippers operating largely or wholly in the LSP sector are protected from the impacts of their poor performance by this cross subsidy. The effect of this is that LSP Shipper / Suppliers are not incentivised to address issues such as theft in the same was as Shipper / Suppliers in the Small Medium Enterprise (SME) or Domestic Sector are, consequently they are not incentivised to invest in systems and processes in to the same level, thus distorting costs.

It is an established precedent that Modifications which improve the accuracy of cost allocations can be regarded as better facilitating competition. Ofgem have directed a number of Modifications be implemented on this basis, including Network Code Modification 640, UNC Modifications 94, and 95 and136v.

In their decision letters for these Modifications Ofgem agreed with the respondents;

“…who considered that this proposal will better facilitate relevant objective (d), the securing of effective competition between relevant shippers and relevant suppliers.”

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*.*

This approach results in minimal change to the current code rules and allows for future amendments to the level of allocation to be made to an appendix rather than requiring regular legal re-drafting and associated review; thus promoting efficiency in the administration of the UNC.

If you have any questions in relation to this representation, please don’t hesitate to contact me.

Regards,

Mitch Donnelly

Regulatory Manager