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Dear John,

**RE: MODIFICATION PROPOSAL 0229**

British Gas does not support the implementation of this proposal. We are encouraged to see to see LSP shippers attempt to address present deficiencies in the way that gas imbalance costs are allocated. However, despite feedback from industry, this proposal is unworkable. For example, the process for appointing agents required by the modification is non compliant with EU procurement legislation, agreement would be required as to contractual liabilities between shippers and transporters that are still widely disputed, and the mechanisms for identifying and allocating RbD costs are overly rigid. We are therefore not convinced that this modification represents anything other than an attempt to delay the inevitable removal of cross subsidies that LSP shippers benefit from.

This proposal has not developed as an alternate proposal to modification 228. We are disappointed that despite this SGD have persistently positioned their modification as an alternate to 228/A. There are a number of issues which have not been resolved by SGD which we believe make this proposal unworkable in its current form. Further, these will exasperate already protracted timescales for implementation of this proposal. In our opinion this will result in at least a further two years prior to implementation. It would be unacceptable for the present deficiencies in our industry arrangements to persist for such a long time. Today LSP shippers have no incentive to tackle the causes of RbD, including for example theft and this results in increased costs for consumers.

Because this modification is not an alternate to modifications 194/A and 228/A it must be considered in its own right. Any approval of modification 229 should

not preclude approval of modifications 194/A and or 228/A. Indeed it may be considered appropriate to approve modifications 194/A, 228/A which deliver immediate improvement and for 229 or some derivative of it to form part of a subsequent regime.

If this modification had been workable we would broadly agree with the benefits versus the present regime as set out by the proposer. However because the proposal is unworkable these benefits are false. In addition, given this proposal is not an alternate to modification proposal 194/A 228/A we do not accept that it can claim benefits against them unless or until those proposals are implemented.

We have set out below a more detailed description of the deficiencies of this proposal;

### **1. “Allocation of Unidentified Gas Expert” could be undertaken most effectively and efficiently by xoserve.**

In their proposal, SGD introduce the concept of appointing an Allocation of Unidentified Gas Expert (AUGE). It is then proposed that the AUGE would, using the available data, produce an allocation between the SSP and LSP sectors which does not result in any cross-subsidy between Shippers or Supply Points, does not discriminate between Shippers and facilitates competition between Shippers and Suppliers. We believe that xoserve is independent from shippers. Licence conditions that apply to the services it undertakes on behalf of network owners provide for non discriminatory treatment of shippers. Xoserve is also well placed to deliver these services, it already has access to appropriate information and skilled people. The creation of another industry party introduces additional complexity, and cost and is in our opinion unnecessary. The requirement to spend considerable time to appoint such an expert would only result in a delay in the removal of cross subsidies that the LSP sector presently benefit from.

### **2. The proposed tendering process does not comply with legislation**

SGD have set out a proposed timescale and detailed business rules associated with the tendering and appointment process. SGD’s proposal requires that the UNCC issue an Invitation to Tender (ITT) by the 1<sup>st</sup> October and that completed tenders are submitted by a final date of 1<sup>st</sup> December.

SGD’s proposal makes no recognition that this tender process would be subject to the Utilities Contracts Regulation 2006, which would require the tendering party to receive expressions of interest from parties, either listed on the Utilities Vendor Database (UVDB) or in response to a notice published in the Official Journal of the European Union (OJEU). The Utilities Contracts Regulations require that the tendering party identify suitable companies from the UVDB, and where there are none, issue a notice in the OJEU. The OJEU notice must be in place for a minimum of one month. Following this period, interested parties’ Expressions of Interest would need to be evaluated and

scored and any questions or issues resolved, possibly through presentations by parties to the tendering party, and / or the UNCC. Invitations to tender could only then be issued with a minimum response period of Three weeks.

It is therefore apparent that the proposed business rules, if implemented, would require the Transporters to either be in breach of the UNC timescales or in contravention of the Utilities Contracts Regulations.

### **3. Contracting Liabilities are disputed and unlikely to be readily resolved**

National Grid Distribution issued an open letter to SGD on 20<sup>th</sup> May 2009 setting out their concerns regarding liabilities which they were hoping to address at the Distribution Forum on the 28<sup>th</sup> May. However, we note that this proposal was issued to consultation prior to the Distribution Forum and these issues have still not been addressed.

Transporters are concerned that this proposal would result in them having an obligation to contract with a party, the AUGE, without having full control over the contract terms. In order to address this, National Grid propose that all Shippers could enter into a contract indemnifying the accepting all liability for the acts or omission of the AUGE or that terms could be incorporated into the UNC that would place all liability with Shippers. This is clearly unacceptable to Shippers and would result in a situation whereby Shippers are obliged to enter into a contract accepting unlimited liability for the acts of a third party, over whom they have little or no control.

It is our strongly held view that these issues must be addressed before this proposal can be implemented.

### **4. Implementation will take in excess of 2 years**

There is a perverse incentive upon the LSP shippers to delay implementation of this proposal. This coupled with our experience of industry discussions in this area reinforces our view that implementation will be extremely protracted.

Further to any approval the following activities and timelines are required;

- **Six** months to develop tender document
- **Five** Months to consider tenders and appoint an AUGE
- **Thirteen** months to develop the AUGS and publish charges

Of this, eight months is allocated to industry debate and query of the AUGS. Under the proposal even if no debate is needed, the timelines for the publications of documents ensure that it would take a minimum of two years following implementation before the final charges and AUGS are published.

No mention is made in the proposal regarding when the charges would be effective from, if it was assumed that this would be at the start of the new gas year in October, this would add a further six months from the February charge publication taking the total implementation time to **30 months**.

There is a great deal of precedent for industry discussions about contractual liabilities. For example; User pays contracts themselves took over 18 months to put in place with existing industry parties and without perverse incentives on them to delay. Even now not all parties have signed the User Pays contract.

#### **5. There is no contingency in the event of no AUGE being appointed.**

This proposal would introduce an 'allocation table' similar to that proposed by Corona Energy in their proposal 0194A. At implementation the proposal would populate the table with a zero value, meaning that there would be no reallocation between parties until the AUGE produced and AUGS. The proposal is silent with regards to what would happen if there were either no party tendered to provide an AUGE service, or none of the parties tendering were considered by the UNCC to be suitable.

Our understanding of what would occur in this scenario is as follows;

1. Eleven months is spent developing a tender document and reviewing initial expressions of interest and reviewing submissions. No AUGE is appointed (for example because of contractual terms issues).
2. According to SGD's timelines, a further eleven months would be spent as tender documents and OJEU notice are re-issued (assuming that previous issues have now been addressed) and responses reviewed.
3. Thirteen months are taken by the AUGE to develop the AUGS and for the industry to challenge this before charges are published.

During this **35 month period** no reallocation would occur and the cross-subsidy would persist.

#### **6. The use of flat allocation profile will mean that cross subsidies remain**

SGD's proposal requires that the AUGE produces an AUGS which;

*"Does not result in **any** cross-subsidy between Shippers or Supply Points"*

However, the proposal then goes on to state that;

*"The Monthly Allocation of Energy will be at a flat rate of 1/12 multiplied by the previous month's average SAP."*

Although it can reasonably be argued that Consumer using 'stolen gas' will not burn it efficiently, it must be accepted that there will be a seasonal pattern to theft as consumers, even those engaging in theft, will use more during the winter than in the summer.

The result of this will is that Small Supply Point Shippers will be picking up the **real time** impacts of Theft, which will mean most of the volume will be during the winter period at higher SAP prices.

The reallocation through this proposal would 'smooth' the theft value over the year for the LSP Market, meaning that the winter peaks will be spread over the low SAP cost Summer period. The result of which would be a continued cross-subsidy of the LSP by the SSP Sector.

## **7. The application of the "Allocation Table" is overly rigid**

The key principle behind this proposal has been the introduction of a Neutral third party who will have access to all available data and on an evidential basis produce an AUGS which sets out the 'correct' allocation of energy between the SSP and LSP sectors. However, the proposal then goes on to limit the ability of the AUGS to produce what they may believe to be the most accurate allocation, by introducing specific terms.

Under this proposal the AUGS is required to use the allocation table definitions to identify levels of contribution. Furthermore, the allocation table limits the AUGS to identifying contributions from the Non Daily Metered (NDM) and Daily Metered (DM) Sectors only.

Where the AUGS may identify differences in contribution between NDM sites which have Smart Metering installed, the AUGS is unable to create a differing allocation.

This is in contradiction of the business rule which obliges the AUGS to create an AUGS which; *"does not create a cross - subsidy between meter points"*.

In summary, there are serious flaws that have been identified with this proposal in regards to the contracting and tendering process which remain unanswered. If implemented it is our belief that this proposal would result in contractual uncertainty which may prevent parties from being willing to tender, and would potentially either put Transporters in breach of legislation or require them to breach their obligations under the UNC.

We are disappointed that Shell Gas Direct have chosen to proceed with consultation on this proposal without first addressing these issues.

If you have any questions relating to this proposal, please don't hesitate to contact me on 07789 570 610.

Regards,

Mitch Donnelly  
Regulatory Manager – British Gas