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11 May 2006

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Dear Ndidi

Review of Reconciliation by Difference (RbD)

ScottishPower welcome the opportunity to respond to the Consultation document seeking views on the Reconciliation by Difference (RbD) settlements mechanism and any issues that we believe are having a material impact on the allocation of costs to domestic shippers.

We have provided responses to specific questions raised within the consultation as detailed below:

Section – Introduction

Question 1 – Given the original rationale and benefits of RbD, do you consider it remains valid under the current GB Gas arrangements?

Evidence presented within the consultation paper indicates that in aggregate since the inception of RbD, there has been a substantial value of reconciliation volume passed through to the Smaller Supply Point market, with the net allocation value being reconciled in the region of £270m. While reductions in the net allocations are evident with the yearly reporting figures covering the period from 2000 to 2004, a reversal of this position was reported for the period from Feb 2004 to Jan 2005, with a substantial increase being realised at this time. We believe this is down to a number of factors, when taken together, create increased risk to the robustness and equitability of RbD settlement. We will comment in detail on the underlining issues that we believe are having a detrimental impact on RbD within the body of this response.

When the principles behind RbD were agreed allowing for the initial period immediately after the completion of the introduction of domestic competition, it was anticipated that volumes requiring reconciliation would decrease with improvement to data quality. However, volumes requiring reconciliation continue to be unreasonably high and therefore this would suggest that further examination and review are required to test the robustness of the key variables affecting overall meter point accuracy.

From the data presented, it could be viewed that the allocation process has become ineffective in apportioning volumes to the correct market sector and this is impacting the domestic market. Since the inception of RbD, system technology and architecture has advanced. We would consider that if appropriate improvements, through industry change do not achieve the required stability in the level of reconciliation volumes, it may be the time to consider extending meter point reconciliation across the Smaller Supply Point market, similar to the model operated in electricity settlements.

Question 2 – Are the costs and benefits of the RbD process transparent to the industry and if not how can transparency be improved?

ScottishPower believe that currently the costs and benefits of the RbD process are not entirely transparent to the Industry. ScottishPower attend the RbD Sub Group, which meets quarterly to review the data from RbD verification and RbD risk modelling. Extending the scope of data presented could enhance RbD verification and the audience perception of activity inputs and their consequential affect on RbD. Initial suggestions could be additional information relating to the ongoing AQ appeals activities of Shippers and performance reports on Meter Point reconciliation achieved in the Larger Supply Point Market against market share. The inclusion of such information would allow Shippers to form a view regarding the direct RbD impact that these activities were having on their cost allocation.

Question 3 – Do the various RbD related industry work groups provide sufficient governance and transparency of the RbD arrangements?

See comments above.

Question 4 – If there sufficient transparency of the data or the information xoserve provides to the Industry?

xoserve currently publish data relating to RbD volumes on the Shipper Information System (SIS). Accessing this data provides information relating to movements in RbD energy allocations with commentary provided on reasons for adjustments. However, this data is presented through a “lotus notes” application, which is not easily accessible by all Shippers. We believe that transparency of information would be improved if data was presented on the website or on a platform which is accessible to all users systems.

Question 5 – *Is the scope of the current RbD Audit appropriate?*

Further investigation required.

We believe that it would be worthwhile in light of the review, to revisit the scope of the RbD Audit to ensure that it remains fit for purpose.

Question 6 – *Are there sufficient incentives on all parties to limit the size of RbD?*

Modification 640 introduced incentives on Shippers to appeal AQ values in a timely manner where evidence is present that suggests the AQ value currently assigned to a Meter Point is understated. Shippers are penalised if they are not proactive in managing the timely appeal of AQ values where the Meter Point AQ value resides erroneously within the Smaller Supply Point sector.

Filter Failure liabilities are applied on Shippers to ensure that reconciliations due within the Larger Supply Point market are progressed in a timely manner.

However other than those measures mentioned above, there does not appear to be adequate incentives placed on Parties that would facilitate the reduction of RbD reconciliation volumes. Shippers control AQ activity and there is no performance targets on the % of AQ amendments that are processed.

RbD Issues

Question 7 – *Do you consider there is sufficient transparency in the operation and accuracy of industry processes such as AQ review and shrinkage calculations?*

AQ Review

With regard to the AQ Review process, ScottishPower believe that previous additional safeguards and measures introduced through Network Code Modifications, have served to influence Shipper behaviour in relation to amendment activity. However, it could be viewed that the current tolerance levels that apply, which prevent amendments being submitted where the change to the AQ value is greater or less than 20% of the current AQ value, penalise Shippers who have a portfolios mix that include large numbers of customers where small movements in AQ values are justified. Taken in aggregate these amendments if allowed to flow through to settlements could have a marked impact and influence on the accuracy of RbD allocations.

In addition, restrictions on the ability to submit AQ amendments within the Smaller Supply Point market outwith the formal AQ review amendment phase, result in erroneous AQ values being carried forward and maintained until the next AQ Review period. Currently, for Supply Points that transfer during the review period, the incoming Shipper has limited ability to propose amendments. The lack of ability to appeal/amend Meter Points that reside within the Smaller Supply Points market throughout the Gas Year, as is currently available within the Larger Supply Point market, inhibits the accuracy of AQ values. ScottishPower believe that

further debate and discussions are required on the viability of extending the current AQ Appeals process to include Smaller Supply Points.

IGT CSEP NExA - AQ Updates and Large Supply Point Reconciliation Values

ScottishPower have raised a series of Modifications to iGT Network Codes to insert obligations relating to the timely and accurate update of information to Large Transporters. In addition, a UNC Modification has been raised to oblige Large Transporters to process data received from iGTs within given timescales. To avoid obligations residing in both the CSEP NExA and respective Network Codes, a further Modification will be required to UNC to facilitate the removal of obligations currently present within Annex A of the CSEP NEXA. ScottishPower believe that inserting the obligations within Network Code will give Shippers the ability to propose changes to the current process and will result in increased visibility and transparency.

Issues with the provision of AQ update information have been high on the Agenda of the Gas Forum IGT Workgroup for some considerable time. xoserve produce and present reports on a regular basis outlining iGT AQ updates and reconciliation activity. However, due to the data submissions being at Logical Meter Number level, there is no visibility of whether or not all new connection and change of supply activity generated are being updated to xoserve by individual iGTs accurately, in a timely manner and in line with NExA obligations. Complex issues persist with the process including the procedure used for updating Nested CSEPs. Nested CSEPs occur where additional iGTs operate downstream of the original CSEP connection.

For I&C reconciliations, reports produced by xoserve highlight that a number of iGTs have failed to submit any reconciliation values resulting in a large number remaining outstanding. The process for reconciliation is made more complex where a change of supplier exists. If accurate AQ update data has not been passed to the xoserve, the process for reconciliation becomes more difficult, and in some cases, may never take place.

In summary, the above issues contribute to the potential for the misallocation of energy between Shippers and where no updates are processed smearing across RbD Shippers. While Modifications have been proposed to improve aspects of the current process and to increase accountability by iGTs and Large Transporters to perform and process the updates in a timely manner, we firmly believe that a fundamental re-evaluation of the current update process and mechanism is required.

Within the recent Ofgem Consultation document “Conclusions on the review of structure of Gas Distribution Charges” Ofgem considered whether the CSEP Administration charge was cost-reflective and whether the manual processes, which currently underlie this charge, have been efficient. It was concluded that the CSEP Charge accurately reflected the costs incurred by Large Transporters in managing CSEP information under the existing labour intensive processes and that the charge should be kept under review to assess the net benefits of

switching to an automated process. Through analysis of iGT and CSEP invoices, ScottishPower has evidence of a sizeable mismatch in the number of Supply Points invoiced by iGTs against those within the CSEP Invoice. We are undertaking further analysis and will address the issue with the individual iGTs concerned, however this does not take away from the fact that energy misallocations are occurring and when taken in aggregate have the potential to have a detrimental affect on the robustness of RbD.

RGMA

RGMA went live in July 2004. ScottishPower believe that metering data quality has suffered as a result of this, which in turn has a negative effect on RbD reconciliation values. ScottishPower have played an active part in trying to increase the quality of metering data by raising numerous change requests. These have largely been opposed by the Large Transporters to the point where ScottishPower believe there is a certain amount of apathy within the market in relation to raising change requests that are likely to result in changes being required to systems operated on behalf of Large Transporters. Recent evidence suggests that for changes of this nature, the Large Transporters are likely to oppose the change.

Question 8 – Do you consider the existing governance arrangements around these processes to be appropriate?

With regard to the CSEP NExA we do not believe that this is the appropriate mechanism for governance and as outlined above, we have raised a series of Modifications to reference the obligations on both iGTs to provide timely updates and for Large Transporters to process data received in a timely manner with the relevant Network Codes.

Ofgem has now approved a Change Proposal to SPAA, which serves to introduce a set of Governance Rules surrounding the Metering Schedules. It is envisaged that if robust reporting is agreed to monitor performance and adherence to the obligations, improvements in data quality should be seen.

Question 9 – Do you consider there are appropriate incentives in place on relevant parties to ensure the timeliness and accuracy of these processes?

xoserve monitor Shipper use of the Industry AQ Calculator, particularly during the AQ Review process itself. Reporting measures have been developed to monitor Shipper amendment activity that may be deemed to give them a commercial advantage over others with any inappropriate behaviour being reported to Ofgem within the timeframe of the review period. If deemed necessary, Ofgem will then contact individual Shippers to address specific areas of concern. It has been recognised that during the AQ Review for the Gas Year 2004/05 that no formal requirement exists within UNC to monitor Shipper amendment activity during the review period. A UNC Modification Proposal has now been raised to formalise and thereafter develop the reporting requirements. However, there continues to be a reliance on Ofgem to receive and act on any reports ideally within the

timeframe of the AQ amendment phase. While Ofgem's continued involvement is necessary, ScottishPower believe that consideration should be given to further enhancing the accountability and overall assurance of the process by the engagement of independent auditors to overview AQ amendment behaviour and associated activities.

Through a recent Change Proposal approved within the Supply Point Administration Agreement (SPAA), Suppliers have put measures in place to ensure the accuracy of metering data and that the relevant parties are updated in a timely manner. However, there are a number of issues with Large Transporter systems that inhibit the update of meter asset data.

Question 10 – Do you consider that the timing and scope of the AQ Review is appropriate

As mentioned previously, ScottishPower believe that the AQ Appeals process should be extended to include Meter Points that reside within the Smaller Supply Point market. It is also our view that the frequency of AQ calculations needs to be reconsidered. While at this time we are not advocating full Meter Point reconciliation, we do believe that a number of additional measures could be developed to alleviate the risk to the level and impact of reconciliation volumes entering RbD. The concept of rolling AQ values for Larger Supply Points, which would result in the recalculation of the AQ value on receipt of a valid meter reading should be investigated and properly evaluated to determine the extent of benefits that could be delivered by adopting such an approach.

Wider Considerations

Question 11 – What would the likely costs of introducing Meter Point reconciliation to all supply points?

ScottishPower believe that the introduction of individual Meter Point reconciliations would bring financial certainty to Domestic Shippers, as they would only pick up costs, which were appropriate for their portfolio. Based on the information presented by Ofgem within the Consultation document, it could be viewed that the current value of RbD reconciliations within the Smaller Supply Point market could act as a barrier to competition. It could be viewed that the risk to small players considering entry to the market is substantial. However, the potential complexity of the Industry moving to individual Meter Point reconciliation would need to be thoroughly evaluated and therefore at this time it is difficult to determine what the likely costs would be.

Question 12 – What conditions would need to be satisfied in order for individual Meter Point reconciliation to be practicable?

The Industry would need to establish if deliverable and sustainable benefits could be achieved when weighted up against the potential costs prior to any decision being made on moving to individual Meter Point reconciliation.

Question 13 – *Would it be feasible for shippers to choose whether their supply point should be individually reconciled or processes through RbD?*

ScottishPower believe that it would make the process more difficult to manage if only certain groups within the Domestic market were individually reconciled and RbD covered others.

SUMMARY

ScottishPower believe that the original principles underpinning the operation of RbD are sound. However, market conditions have developed since the time of RbD introduction, which now need to be considered when evaluating if RbD remains the most effective and reliable method of allocating and managing energy allocations within the Small Supply Point market. While at this time we are not advocating a move to individual Meter Point reconciliation, we do believe that there are a number of factors that collectively are having undue influence on the materiality of reconciliation values being applied to the Smaller Supply Point market through RbD settlement.

We believe that the issues raised within the consultation and those highlighted by Shippers and Interest Parties require to be examined in greater detail. Where improvements can be made through Industry change, these should be taken forward and driven through the formal change process. We firmly support changes that will bring about added certainty and assurance within the process and to the market environment being pursued. However as the majority of the risk with adverse RbD reconciliations rest with RbD Shippers, the required change may be difficult to achieve if the support of those parties who could be regarded as being neutral in the process are not assured.

If you wish to discuss any points raised in this response, please contact me on the above telephone number.

Kind regards

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