

# The Creation of a Revenue Protection Activity Co-ordination Agent (RPACA) and a Central Revenue Protection Unit (CRPU)

Two Proposals from British Gas combining the Supplier Energy Theft Scheme Model (SETS), the Theft Code of Practice, and new service provider(s) tasked with delivering co-ordination and optional services.

<b>Author(s)</b>	David Watson, British Gas
<b>Document Status</b>	Final
<b>Document Version</b>	v1.0
<b>Date Issued</b>	8 <sup>th</sup> April 2011

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## EXECUTIVE SUMMARY

1. Detecting theft of gas is an important activity in the UK gas market. We estimate that approximately £220m of gas is stolen each year with the costs being borne entirely by the wider, law-abiding, domestic customer in the form of higher charges. Importantly it also places the lives of those who steal and those in the vicinity at serious risk. We are aware of a number of cases where undetected theft has led to gas safety incidents in which members of the public have been either seriously injured or have lost their lives. We believe industry parties have a responsibility to maintain the safety of the network and that an integral part of this involves the detection and resolution of theft.
2. Against this context we consider that most Suppliers do not take sufficient action to detect the theft which exists on their portfolio, and that this is a direct consequence of the lack of commercial incentives these Suppliers face, which in turn makes taking action more difficult. For example, the current industry settlement rules mean that for each £1.00 of detected gas theft, most Suppliers will only save a small amount in avoided future cost with little prospect of actually recovering the lost revenue. This means that, when faced with the large expense of financing a Revenue Protection service Suppliers find it does not make commercial sense to detect and resolve theft, and consequentially most do not make sufficient investment.
3. This is evidenced by the industry statistics on Shipper theft detection performance published by the Gas Network Owners each month<sup>1</sup>. In 2009 for example, British Gas detected 83% of all theft in the market despite having only a market share of just over 40%, with the next best performing Shipper detecting just 4%. By 2010, this situation had only marginally improved with British Gas detecting 77% of all theft in the market with the next best performing Shipper detecting just 6%. The responses to a recent Ofgem questionnaire on the subject similarly highlighted issues with the current situation, with British Gas responsible for as much as 84% of all investigations of suspected theft, detecting as much as 87% of all stolen gas in energy terms and employing up to 85% of all Revenue Protection staff used in the market. These figures should be seen the context of the fact that of the all the leads reported to Suppliers, xoserve statistics show that only 33% related to British Gas' sites. We believe this not only highlights the size of the issue which these commercial disincentives have created, but also the leadership position we have taken on addressing gas theft.
4. The Supplier Energy Theft Scheme (SETS) proposed by British Gas<sup>2</sup> fixes this issue by linking, in part, Suppliers' financial performance to their

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<sup>1</sup> Under Standard Licence Condition 17.3, Suppliers must report all suspected cases of theft to the Network Owner. These reports are collated, along with the outcomes of any investigation in the monthly xoserve Theft of Gas Statistics.

<sup>2</sup> The SETS was proposed under UNC Modification Proposals 0277 and 0346. Links to the documents can be found [here](#).

performance in detecting theft. This ensures that Suppliers have a stake in the results they deliver and are therefore incentivised to invest in the detection of gas theft.

5. The SETS will incentivise all parties, including those who do not presently wish to act. These parties say that their performance in detecting gas theft should not be linked to financial consequences and that instead the industry should create a new centralised monopoly named the National Revenue Protection Service (NRPS)<sup>3</sup> who will handle theft detection on their behalf, with no link between its performance in detecting theft and their financial performance. By its very nature, we believe the SETS will be resisted by those who it seeks to incentivise and argue that the resistance to the SETS and the protracted development of alternative proposals could be motivated by a desire to stop or delay investment in theft detection activities.
6. Generating good quality leads is the comparatively easy aspect of theft detection with the turning of those leads to actual detected theft presenting the real challenge. It is for this reason that 88% of our Revenue Protection staff are employed on investigation activity rather than lead generation. The methods used to steal gas can be remedied by the customer in a matter of seconds meaning that, unlike electricity theft, theft of gas often requires catching the offender red handed and therefore means calling and gaining access at exactly the right time. It is far easier not to detect theft than to detect it and it is for this reason why a licence obligation to investigate or detect theft would be unenforceable.
7. Whilst SETS solves this issue by incentivising those Suppliers who ordinarily would not act, we recognise that some revenue protection services would benefit from centralisation, specifically where either they cannot be provided by the competitive market or when the incremental benefit of centralisation outweighs the benefit of provision by the competitive market. The proposals contained within this document therefore seek to provide for some optimisation above and beyond the SETS by providing this missing element by combining three competing industry proposals on theft reform in order to form a holistic solution. Specifically, under these proposals the existing Supplier Energy Theft Scheme (SETS) proposed by British Gas and the Code of Practice for Theft Detection being developed under the Distribution Connection Use of System Agreement (DCUSA) Change Proposal 054 Working Group would be combined with one of two new models for an industry Revenue Protection Service;
  - a. Proposal One: the creation of a “Revenue Protection Activity Co-ordination Agent” (RPACA) who would provide the services which would benefit from centralisation, referred to throughout this document as “Co-ordination services” and

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<sup>3</sup> The papers for the Gas Forum's NRPS Working Group can be found [here](#).

- b. Proposal Two: the creation of the RPACA referred to above plus the creation of a Central Revenue Protection Unit (CRPU) who would enter the competitive market to provide those services which do not form a natural monopoly or are best delivered by the competitive market, referred to throughout this document as “Optional services”.
8. Specifically our proposals for an RPACA to provide Co-ordination services include provisions for the collection, collation and dissemination of management information on where theft is and how it occurs, the provision and management of a National Theft Hotline, the management of a stolen meters register, the co-ordination of the hand-over of investigations between Suppliers during the change of Supplier process, the facilitation of discussion between the industry and non-industry agencies with an interest in gas theft and the collation and sharing of best practice from around the industry. We consider these to all be important elements for the future detection of theft, yet may not be adequately provided by the competitive market.
9. We recognise however that some may argue that not all Suppliers have equal access to fit for purpose value for money Revenue Protection Services and that the combination of the SETS and the Co-ordination services detailed in Proposal One may not be sufficient to provide theft reform which will work for everyone. We have therefore also included within this document a second proposal, Proposal Two, provides for both the RPACA referred to in Proposal One and the creation of a CRPU which would enter the existing competitive market for the provision of Optional services. These services include the collection and processing of data for the purposes of lead generation and risk profiling, field services for physically detecting and resolving theft, the provision of debt and revenue recovery services, the provision of legal services, the provision of settlement management services and the ongoing management of sites where theft has occurred. For clarity, both the RPACA and CRPU models are intended to compliment the SETS and not replace it.
10. The Optional services detailed in Proposal Two can all be adequately provided by the market if Suppliers were incentivised to procure or provide them, however as we have already detailed that is not currently the case in the gas market. We therefore also propose that the SETS model proposed by UNC Modification 0277 or 0346 is implemented alongside either Proposal One or Proposal Two, incentivising Suppliers to detect theft on their portfolio through working with the RPACA in relation to Co-ordination services, and by either contracting with the CRPU, or finding an alternative provision, for Optional services.
11. Furthermore, we propose that regardless of whether Suppliers contract with the CRPU or not for Optional services, all Suppliers will be obligated to ensure that the parties they engage with adhere to the provisions of the Code of Practice. This ensures that the customer treatments will be standardised across the entire industry, regardless of how a Supplier manages the theft on their portfolio.

12. We contend that these proposals, combined with SETS and the Code of Practice, deliver all the advantages of the NRPS model developed under the Gas Forum without the disadvantages. By linking Suppliers' financial performance to their theft detection performance, the volume of theft detected will increase. This in turn will improve customer safety and reduce the costs that the law-abiding public pay from the theft of others. This proposal not only secures that increase in the volume of theft detected, but also provides Suppliers with the means through which to achieve those reductions, enabling parties to procure a service which fits their needs, as well as providing a central focus for co-ordinating activities and the sharing of intelligence and best practice. The effect of these two proposals are to ensure that Suppliers' financial returns are linked in part to their theft detection performance, that all Suppliers have access to the cost effective means with which to detect that theft, that measures are put in place to standardise the treatment of customers and that revenue protection services which can be appropriately monopolised are delivered by a centralised, regulated, body.
13. The NRPS proposed by our competitors by contrast will not achieve these aims as it seeks to rely on obligations alone to ensure parties engage in Revenue Protection activities and furthermore centralises a large proportion of the revenue protection market, despite many of these services not forming a natural monopoly. Specifically, their proposals explicitly fail to recognise that in a market where the marginal benefit of theft detection is generally negative, mechanisms must be found to ensure that Suppliers to commercially want to drive down the amount of theft and therefore share in the outcomes financially.
14. We therefore recommend that following the forthcoming Theft Impact Assessment, Ofgem direct the implementation of the SETS under either UNC Modification Proposal 0277 or 0346, the Theft Code of Practice and direct the necessary steps to implement either Proposal One or Proposal Two of this document.

## **STRUCTURE OF THIS PROPOSAL**

15. Before providing the detail behind this proposal, we have set out some background to the current position and the case for change, including why we believe an alternative proposal is required.
16. The document then goes on to set out in turn the details behind Proposal One, for the RPACA, and then Proposal Two, the RPACA and CRPU. Please note that although they are two distinct proposals, aspects such as the scope, governance, funding and benefits of both proposals are addressed together within this document for ease of reference.

# INTRODUCTION

## Background

17. Following two Ofgem consultations in 2004 and 2005 respectively on the future of theft reform<sup>4</sup>, the ERA and ENA commissioned a joint working group, the Theft of Energy Working Group, to look at theft reform and develop recommendations which could be progressed. Their report was published in April 2006.
18. The Theft of Energy Working Group report concluded that theft may not be being dealt with effectively because *“industry participants may be commercially disincentivised, obligations may not fall where they would be best placed, there may no longer be a common baseline for quality of service because of the introduction of multiple agents, information may not flow between competing suppliers and their agents, meaning that the change of supplier process itself could undermine the effectiveness of revenue protection work”*<sup>5</sup>. They then proceeded to recommend that *“obligations on parties”* to detect theft should be introduced, *“incentives”* should be developed and a *“Code of Practice”* should be adopted<sup>6</sup>.
19. British Gas subsequently raised UNC Review Group 0245<sup>7</sup> in to look at the options for theft of gas reform and develop solutions. This group’s final report made a number of recommendations, including that two specific models be developed further; a Supplier Energy Theft Scheme (SETS) incentive scheme and a National Revenue Protection Service (NRPS) concept which would centralise provision of some revenue protection services.
20. As a result of this report, e.On raised UNC Modification Proposal 0274 with a view to further developing the NRPS concept and British Gas raised UNC Modification Proposal 0277 to further develop the SETS. Whilst the former now continues to be developed outside of industry code governance under the auspices of the Gas Forum, two different versions of the SETS has now been fully developed and submitted to Ofgem for consideration under UNC Modification Proposals 0277 and 0346.
21. Ofgem have announced that they will be releasing a Theft Impact Assessment in the near future which seeks views on each of the proposals for reform, before finally making a decision over which package of options

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<sup>4</sup> Theft of Electricity and Gas - Discussion Document, April 2004, Theft of Electricity and Gas - Next Steps, January 2005

<sup>5</sup> ERA / ENA Report, page 2, summary.

<sup>6</sup> ERA / ENA Report, page 3, summary of recommendations.

<sup>7</sup> The papers for this Review Group can be found [here](#).

was most suitable. These proposals are the latest options to be developed for inclusion in that assessment.

## The Case for Change

22. The exact volume of stolen gas is not known, and estimates in the industry vary considerably. From our analysis of unidentified gas figures however, we estimate that as much as £220m of gas is stolen each year. Because stolen gas is largely paid for by the remaining, law-abiding, population, prices levied on the many are unnecessarily high as a result of the actions of a few.
23. It is also accepted that theft of gas is inherently dangerous, with thieves tampering with or bypassing equipment which is designed to regulate the flow of gas to a property. This can, and has, led to numerous serious incidents including gas leaks, explosions and carbon monoxide escapes which have all caused injury or death to those in the vicinity.
24. Against this backdrop, the statistics published by the Gas Network Owners on the number of theft detections which are reported to them<sup>8</sup> show an extremely poor level of detection activity. In 2009 for example, British Gas detected 83% of all theft in the market despite having only a market share of just over 40%, with the next best performing Shipper detecting just 4%. By 2010, this situation had only marginally improved with British Gas detecting 77% of all theft in the market with the next best performing Shipper detecting just 6%. The responses to a recent Ofgem questionnaire on the subject reinforced this picture, highlighting that British Gas are responsible for as much as 84% of all investigations of suspected theft, detected as much as 87% of all stolen gas in energy terms and employed up to 85% of all Revenue Protection staff used in the market. These figures should be seen the context of the fact that xoserve statistics show that only around 33% of the theft of gas leads provided to Suppliers related to British Gas sites.
25. The ERA / ENA Working Group found that one of the primary reasons why this situation has occurred is that many Suppliers are “*commercially disincentivised*”<sup>9</sup> from detecting theft by the way in which the costs of theft are settled within the gas market, and thus the current problems in the market arise from a lack of appropriate financial incentives.
26. In the Small Supply Point (SSP, largely domestic) market Suppliers pay for their gas based on an estimate of the amount of energy the customer is believed to be using, known as the “AQ”. In the vast majority of theft cases, the AQ will be artificially low as any readings from the site will be no longer be recording all the consumption. Although the Supplier will continue to pay

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<sup>8</sup> Under Standard Licence Condition 17.3, Suppliers must report all suspected cases of theft to the Network Owner. These reports are collated, along with the outcomes of any investigation in the monthly xoserve Theft of Gas Statistics.

<sup>9</sup> ERA / ENA Report, page 2, summary.



for the energy up to the value of the AQ, the energy over and above this will not be allocated to the Supplier in question and will instead be borne by the wider SSP market, with SSP Suppliers picking up a share of those costs in proportion to their market share of SSP Supply Points.

27. In the Large Supply Point (LSP, largely non-domestic) sector, Suppliers pay for their gas based on the actual meter readings returned from the site, meaning that all stolen energy will be misallocated. Again, these costs are borne by the SSP market with SSP Suppliers picking up a share of those costs in proportion to their market share of SSP Supply Points.<sup>10</sup>
28. As a result, if British Gas prevents £1.00 of stolen gas being misallocated in the market, they save over £0.40. A Supplier with 5% market share however would only save £0.05 for every £1.00 of stolen gas they prevent from being misallocated.
29. This is compounded by the fact that resolving gas theft is both difficult and expensive. Gas can be stolen in ways which leave no trace of the theft and many types of theft can be made good in a matter of seconds, meaning that Suppliers need to spend both time and money catching the customer in the act. A good example of this, and a situation commonly found, is the use of substitute meters which capture the majority of consumption before being exchanged back out by the culprit before a meter reading visit. This type of theft can be corrected in less than thirty seconds without leaving any markings on the “official” meter. Another notable example is the way in which the gas prepayment meter housing can be interfered with a piece of plastic so that it passes unlimited gas. The tamper can be inserted and removed instantaneously without leaving evidence behind. Detecting this type of theft takes more time, effort and cost than simply visiting the site
30. It also follows, therefore, that simply obligating Suppliers to tackle theft without linking the results they deliver to their commercial performance will not work as it will be very easy for them to make a “token” effort to achieve compliance without actually making progress.
31. Given both the poor rewards for detecting gas theft and the high cost associated the practice of detection itself, it is perhaps no surprise that so many Suppliers choose to do nothing. We therefore consider that without change the commercial disincentives to act will continue to exist and some Suppliers will continue to make choices which are not in the interests of the wider market.

## **The Need for an Alternative**

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<sup>10</sup> Modification Proposal 0229 will shortly change the way in which the costs of LSP theft are allocated, with an independent expert developing a methodology to assess where the costs originated and then allocate them accordingly.

32. The Supplier Energy Theft Scheme (SETS) resolves the issue of commercial incentives by linking, in part, Suppliers' performance in theft detection with their overall financial performance, such that it makes commercial sense to invest in theft detection, if not to improve customer safety and avoid the socialisation of charges then to avoid financial penalties associated with poor theft detection performance.
33. Whilst the SETS will therefore incentivise those who would not ordinarily invest in theft detection activities, we recognise there is a role for the centralised provision of some revenue protection related services in the market, specifically where either those services form a natural monopoly or where centralisation would deliver incremental benefits which outweigh the benefits delivered by the competitive market. The current SETS proposals on their own do not address this, and we have therefore set out in both Proposal One and Two of this document provisions for a Revenue Protection Activity Co-ordination Agent (RPACA) will provide the Co-ordination services the market cannot adequately do, improving the extent to which theft detection efforts are co-ordinated across the industry..
34. We also recognise that some may argue that not all Suppliers have access to the Revenue Protection services through which to adequately deliver theft detection services. We have therefore included within this document Proposal Two which, in addition to the RPACA, provides for a Central Revenue Protection Unit (CRPU) who would enter the competitive revenue protection market and offer Optional services to any Suppliers wishing to contract with them. Our intention is that the combination of the SETS, the Theft Code of Practice currently under development, the Co-ordination services of the RPACA and the potential for the Optional services of the CRPU can serve as a holistic solution for theft reform.
35. Although the NRPS proposal being developed under the Gas Forum purports to also provide this by obliging Suppliers to sign up to a centralised Revenue Protection agency, we argue that will not work because it lacks the financial incentives necessary for Suppliers to genuinely want to work with the new body to detect theft. We consider the effect of this is that Suppliers, now fully compliant with the relevant regulations and statutes by virtue of the existence of the NRPS, will be incentivised to minimise their financial exposure to it. This can be achieved in a number of ways, for example limiting the amount of engagement they have with the NRPS, reducing the amount of co-operation they provide to the NRPS, restricting the amount of data provided and the frequency with which it is provided to the NRPS, preventing any future change or innovation which may increase costs and under-resource any Nominated service elements in the same way that happens now.
36. We note that the existing NRPS proposal provides for some assurance processes to be created so that Suppliers can be held accountable, however we consider that such an audit regime would need to be both unreasonably large and intrusive to determine whether a Supplier was taking only token efforts to detect theft as opposed to genuinely addressing the issue. As a

result, proposal developed under the Gas Forum contains assurance processes we consider weak and ineffective. Ultimately, Suppliers will never be truly interested in the outcome of theft detection until they have a financial interest in seeing it successfully detected. Why, for example, if the proponents of the NRPS proposal are serious about resolving theft would they be so reluctant to take a financial stake in the results which it delivers?

37. Finally, we also note the significant legal issues associated with the NRPS proposal as currently developed under the Gas Forum, specifically in relation to the Data Protection Act (1998). Our legal advice, provided to the Gas Forum and attached to this proposal as Appendix Two, indicates that the assumption that Suppliers can simply provide large amounts of personal data to a third party service provider is flawed, and may lead to a breach of Suppliers' obligations under primary legislation.

## **SCOPE**

38. This scope of these proposals are limited to the gas market only at this time, although it is our intention that any Co-ordination or Optional services offered by any new body should be available to all gas Suppliers, regardless of which customer type or segment they serve.
39. We are however mindful of the discussions currently underway in the electricity industry regarding theft reform there, and want to make clear that both proposals have been designed so that, at some future point in time, they can provide a dual-fuel solution. Indeed, we note that each of the elements in our vision, the SETS, the Code of Practice, the RPACA and the CRPU are all equally applicable to both the gas and electricity markets.
40. Finally, we also consider that at some point in the future, it is conceivable that these proposals may also be extended to provide solutions for theft from the Network, otherwise known as theft in the course of conveyance.

## **THE PRIMARY OBJECTIVES OF THE RPACA AND CRPU**

41. Our proposal is that both the RPACA and the CRPU will be guided by primary objectives, and that both the way each develops and their overall performance will be assessed against them. Specifically, these primary objectives are:
  - a. To facilitate the detection of theft, and
  - b. To prevent and deter theft
  - c. In a way which does not unduly discriminate between the Suppliers to whom the services are provided to.

## **PROPOSAL ONE: THE REVENUE PROTECTION ACTIVITY CO-ORDINATION AGENCY (RPACA)**

42. Our first proposal is for the creation of the RPACA who will take on the role of providing Co-ordination services which we consider the competitive market is not able to adequately provide by itself. These services will be mandatory for the RPACA to provide and must be provided to all Suppliers in a non-discriminatory way. This section set out those services in more detail.

### **Management Information on Theft**

43. Currently the information Suppliers collect during the course of detecting theft is largely retained internally for the purposes of both resolving the customer elements associated with the theft detection and informing future theft detection strategies. In addition, a small amount of data is also shared with the Network Owner in order to satisfy obligations under the Standard Licence Condition 17.3 of the Supply Licence.
44. We believe that information on the outputs of theft detection can aid all Suppliers in detecting more theft and more should therefore be done to share information. Whereas sharing the “input” data such as payment history, meter read data, bank account details, customer name and MPRN for the entire UK market is prohibited under the Data Protection Act (1998), sharing the “output” data, the who, what, where and how, from confirmed theft detections is not<sup>11</sup>.
45. By sharing this data Suppliers can make better decisions about how they use the resource available to them, reducing the marginal cost associated with theft detection in the process. Additionally they will also be able to adjust their approach according to the circumstances at hand. For example, information which enables Suppliers to see how theft occurs in different geographic regions is highly valuable and can in itself lead to a consequential increase in the volume of theft detected.
46. Specifically it is our proposal that Suppliers are obligated to collect the following data items whenever they find a confirmed case of theft, and report them to the RPACA for them to store, collate and issue out as a monthly report to industry participants no later than twenty-eight days after the end of the reporting period.
- a) Address,
  - b) Meter Point Reference Number (MPRN),
  - c) The offence committed, as defined in the Gas Act (1986),

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<sup>11</sup> This is expanded upon within our legal advice provided to the Gas Forum, attached in Appendix Two.

- d) How that offence was committed,
  - e) The date of detection and the period of time which the Supplier assesses the offence was committed between, and
  - f) The assessed value of any gas deemed to have been stolen.
47. For clarity, we have not defined how this data will be shared with the RPACA as we consider that the mechanism will need to be defined once they have been appointed, although note that if the Network Owners or their agent were to take on the role of providing Co-ordination services, the existing Conquest Theft of Gas form could be used.

### **Stolen Meters Register**

48. We also propose that Suppliers should be obliged to log details of any meters which they, or their agents, find to be missing or stolen with the RPACA so that a register may be compiled, and then shared with industry participants. We consider that such information would prove valuable to Suppliers and their agents in the course of their theft detection activities, especially when attempting to determine whether a meter they have found on site is being used as a “substitute meter” in the course of theft, or whether it is simply a meter exchange which they have not been informed about.
49. For clarity, we have not defined how this data will be shared with the RPACA as we consider that the mechanism will need to be defined once they have been appointed.

### **Public Information and the National Theft Hotline**

50. We believe there is a general lack of co-ordination about the industry’s approach to encouraging the public to provide information on where theft may be occurring. We are aware that leads are currently provided to Suppliers, Network Owners, consumer bodies, the Police, the UK Revenue Protection Agency, Ofgem and others but consider that this fragmented approach relies more on members of the public knowing about the dangers associated with gas theft, knowing who to contact and then having the will to do so.
51. We believe there is a role for a central body, the RPACA, to spearhead the industry’s campaign to highlight the dangers of gas theft with the public, encourage them to provide tip offs and to manage a route for those tip offs to be collected. Specifically we propose that as part of meeting its objective to deter gas theft, the RPACA should be obligated to provide both a National Theft Hotline and to co-ordinate industry wide efforts to publicise the dangers of gas theft and the need to report suspicions of gas theft to the National Theft Hotline.

52. Whilst we recognise that we cannot obligate members of the public to use one single point of contact for such tip-offs, we believe that there is a role for a central body in trying to spearhead this effort, and cite the success of the Government's "Benefit Fraud Hotline" in collecting tip-offs about people who are abusing the welfare system.

### **Change of Supply Co-ordination**

53. Whilst we have not seen any evidence to demonstrate that people under investigation for theft of gas evade detection by transferring supplier, we acknowledge that it is theoretically possible. To that end we consider that the RPACA could have a role to play in providing a solution if and when this does happen.
54. We therefore propose that Suppliers are obligated, on losing a site, to notify the RPACA of any ongoing investigations into potential theft of gas. We also propose that the RPACA will then be required to notify the new Supplier of that ongoing investigation so that Supplier can take appropriate action to establish whether theft is occurring or not. Please note that in order to facilitate this exchange of information we intend to allow the Network Owners to pass details of the current Supplier to the RPACA on request. For the sake of clarity, we are not proposing that any industry flows are created or modified to support this change and instead believe that as the volumes of information expected to be sent is low, email will suffice.

### **Co-ordination with other bodies**

55. There are many other organisations with an interest in resolving gas theft, and our experience is that co-operating with them can increase the volumes of theft detected thus delivering greater benefit. Such organisations include the Police, the Home Office, CIFAS, the Serious Organised Crime Agency, the Association of Meter Operators and the UK Revenue Protection Association. Current co-ordination of effort between these parties is currently fragmented, haphazard and reliant on Suppliers to co-ordinate efforts individually.
56. We consider there is a role for the RPACA to play in assuming the co-ordinating role on behalf of the industry, so that industry efforts to detect theft are more effective. This will be achieved under our proposal by requiring the RPACA to identify other bodies with an interest in detecting gas theft and managing the industry's relationship with those bodies such that our efforts are co-ordinated. We consider this to be an integral part of how the RPACA meets its objective of detecting, prevent and deter gas theft.

### **Best Practice Forum**

57. Whilst the fact that Suppliers retain accountability for managing theft on their portfolio is an intrinsic part of this proposal, we recognise there is benefit in industry parties sharing both best practice and intelligence on emerging

risks, issues and opportunities in relation to theft detection. To that extent we are proposing that the RPACA facilitate fora where this information can be shared on a regular basis, between interested parties from inside and outside of the industry.

### **Delivery options for Co-ordination Services**

58. There are two distinct delivery options for the provision of Co-ordination services under this proposal. The first is that the Network Owners or their agent, xoserve, assume the role of the RPACA on a User Pays basis. The second is that they are provided by one or more Service Providers, selected following a commercial tender exercise.
59. The first option allows for a potentially quicker implementation route, as we consider that the Network Owners and their agent already have substantially the systems or processes required to fulfil the role. This is illustrated within Appendix One of this proposal. In order to deliver the Co-ordination services under this option we consider that a SPAA Change Proposal and a new User Pays service would be required in order to give both the Network Owners an obligation to provide the services and the payment with which to fund that activity.
60. The second option involves a competitive tender and so may potentially deliver greater value for money, albeit at the expense of a longer timeline. This would involve business rules being drafted, a tender being issued and then potentially new services being built with the winning provider, assuming they did not have a ready made capability to provide these Co-ordination services.
61. Although we favour the first option for both its simplicity, speed of implementation and use of existing processes, we include both options within this paper for consideration.

### **PROPOSAL TWO: THE REVENUE PROTECTION ACTIVITY CO-ORDINATION AGENCY (RPACA) AND THE CENTRAL REVENUE PROTECTION UNIT (CRPU)**

62. We recognise that some may argue that the provision of the SETS and the RPACA proposal detailed within this document may leave some smaller Suppliers, or those with a disparate customer base, unable to access Revenue Protection services at a cost which provides them sufficient value for money. Whilst we consider that there are a number of existing service providers who are able to help parties provide bespoke revenue protection provision whatever their shape or size, and argue that the increase in demand for services brought about by the introduction of the SETS will encourage more service providers to enter the market, we recognise that as much assistance as possible should be given in facilitating the Revenue Protection market.

63. We are therefore raising Proposal Two which will, in addition to the provision of Co-ordination services through an RPACA as described above, would provide for a CRPU which will be obliged to enter the Revenue Protection market and offer Optional services to those industry parties who wish to procure them. This will enable those Suppliers unable to procure value for money services from elsewhere with the opportunity to take advantage of the potential economies of scale the CRPU could offer were they to enter the competitive market. For clarity, this second Proposal has been designed to complement both the provision the SETS and of the Co-ordination services detailed in the proposal above. It is not our intention that it should be provided in isolation.
64. We consider the added provision of Optional services could have a number of benefits over the NRPS' proposal to prescribe how Suppliers or their appointed agent should complete activities such as field work. For clarity, the term "service provider" below is taken to mean either the CRPU or any other provider a Supplier contracts with.
- a) Allows Suppliers and their service provider to agree how the service will be provided, ensuring that whatever solution is tailored to meet the requirements of the Supplier concerned and taking advantage of any bespoke data or reports that Supplier may have, or ensuring that any niche the Supplier may operate within is appropriately addressed.
  - b) Enables Suppliers to ensure that the service they receive is appropriately priced, giving maximum value for money. Whilst they will be incentivised to ensure that their service provider delivers the best possible theft detection results, they will have the ability to directly control the cost they face, hedging that investment against potential exposure to the incentive mechanism.
  - c) Provides for much quicker change control. On a bi-lateral basis, a service provider and a contracting Supplier will be able to trial new ideas and data without having to first having to secure an industry change proposal which allows for it. In theory, a Supplier could set up a new process immediately with a service provider under this model to see the effect it had on theft detections. This is not the case with the proposal made by the Gas Forum which would instead require Suppliers to raise, develop and agree with competitors an industry change proposal. Indeed, we note that it is only under this model that a Supplier would share in the success of innovation, and therefore be both incentivised to explore new possibilities and agile enough to deliver it.
  - d) The obligation on the CRPU to provide these services without a corresponding obligation on Suppliers to take up the services will incentivise the CRPU to provide cost effective, innovative and high performing services which will compete with the other service providers in the market. We consider this increase in competition will have benefits wider than on just the CRPU, with other service providers having to similarly improve their offering.



e) The obligation on the CRPU to provide these services also provides insurance against other service providers leaving the market at some point in the future. This ensures that Suppliers will always have the ability to procure data collection and lead generation services.

65. As, under this proposal, the Supplier retains full accountability for the management of theft on their portfolio, it will be for them to agree with the CRPU the key performance indicators and performance targets which they will work to. Unlike the NRPS proposal being developed by the Gas Forum Suppliers will have the flexibility to balance cost and performance as they see fit, with no requirement to provide the same service as the CRPU would provide if they opt-out of taking Optional services from the CRPU. Instead, we propose that performance is instead driven by the SETS incentive mechanism. This mechanism ensures that Suppliers have a direct commercial interest in results which are delivered, howsoever they are delivered. The only caveat to this principle is that all service providers, including the CRPU, will be obligated to adhere to the Theft Code of Practice which dictates the minimum standards which must be met in terms of customer treatment, something which under the SETS proposal, compliance against will be audited to ensure that all customers are being treated fairly.

#### **Data Collection and Lead Generation**

66. It is recognised in industry that the best results in terms of theft detections come when you analyse the available data, held internally and externally, to assess where the risk of theft is greatest and deploy your resources accordingly. The available data for this purpose is vast; in addition to the internally held data items which Suppliers have on their systems it is possible to overlay that with externally procured data such as demographic information, land registry values, financial and credit worthiness data, previous related offences and more.

67. We agree with the Gas Forum proposal that this element of theft detection is absolutely vital to the success of any theft reform. We consider however that a major flaw in the NRPS proposal being developed by the Gas Forum is the incorrect assumption that all Suppliers are able to pass the NRPS any data which is held about it's customer base, regardless of whether there is any grounds for suspicion about that customer and regardless of whether the release of such data is allowed by that Supplier's Privacy Notice<sup>12</sup>.

68. It is our opinion that unless Suppliers amend their Privacy Notices to allow for this release of data, this act would be a breach of the Data Protection Act (1998). This issue is that under the Data Protection Act (1998) any amendment is likely to require an "opt-in" by the customer, essentially making it unworkable in practice. This issue with the NRPS proposal being

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developed under the Gas Forum is explored more within Appendix Two of this proposal.

69. We recognise that some Suppliers may be able to take the steps required to pass the personal data they hold to a service provider, and as such there may be a role for a centrally placed body such as the CRPU to offer data collection and lead generation services. A good example of this are non-domestic Suppliers where the Data Protection Act (1998) does not apply in the same way and the existence of annual contracts mean that Privacy Notices can be changed without a specific “opt-in” process, simply by including any new term at the point of renewal. Domestic customers are fully protected by the Data Protection Act (1998) however, and as such the Suppliers of those customers do not have this luxury. The fact that annual contracts do not exist in this market similarly means that these Suppliers do not have the ability to easily change the terms of the contract without a specific “opt-in” process, unlike in industries such as the insurance or telecommunications market which have annual contracts.
70. Our conclusion therefore is that, as compliance with the Data Protection Act (1998) is the responsibility of each individual Supplier, and that not all Suppliers will be able to take the necessary steps to pass this data to a service provider and comply with the Act, it is entirely inappropriate to obligate Suppliers through their Licence to take data collection and lead generation services from a service provider as the Gas Forum model suggests. To do so would be to give Suppliers a choice between breaching obligations under primary legislation and breaching obligations contained within Supply Licence.
71. We therefore propose that data collection and lead generation services should be offered to Suppliers as a Optional services only, enabling those who can avail themselves of the service from the CRPU to do so if they so wish and leave those who cannot to make alternative arrangements. Whereas this does mean that those Suppliers able to take steps to transfer data to a third party and remain compliant with the Data Protection Act (1998) have more flexibility in approach, we consider that Suppliers individually have the capability to also provide this service internally. This is precisely the solution that British Gas has successfully employed in recent years in response to the legal restrictions we faced in procuring this service.
72. As part of this Proposal, the CRPU will be obliged to provide access to data collection and lead generation services. Any Supplier wishing to contract for those services will bear all the responsibility of ensuring that in doing so the Data Protection Act (1998) is complied with, and for clarity, there will be no obligation on Suppliers to actually take these services from the CRPU.

### **Field Services**

73. Once leads have been generated suggesting where theft may be occurring, it is vital that there is an ability to visit the site in question, establish whether an

offence under the Gas Act (1986) has occurred, collect any evidence, make the situation on site safe and potentially arrange for a new meter to be installed. Such a field service therefore needs to consist of appropriately trained Revenue Protection staff to complete the tasks required of them.

74. We recognise that not all Suppliers have the ability to provide cost effective field services through which theft can physically be detected and resolved. Some small Suppliers for example may have a customer base which is geographically disparate, making it more expensive to provide field services for. Other Suppliers may have a density of customers in one particular geographic area meaning that they may wish to procure bespoke services for all or some of their customer base.
75. We therefore propose that the CRPU be obligated to provide an appropriately trained nationwide field service for those Suppliers willing to contract with them. For clarity, Suppliers will not be obliged to take this service from the CRPU, and any Supplier wishing to contract with the CRPU for this service will be able to do so for all or some of their customer base. This will allow Suppliers the flexibility to procure a service which meets their specific needs. This flexibility extends to the entire service including the Key Performance Indicators or Service Level Agreements used to the number of FTE provided.

### **Debt and Legal Services**

76. Following a detection of theft an assessment of the value of that theft will be made by the service provider. There will then be a need to collect the revenue associated with that theft. By definition, successful theft detection also means that an offence has taken place under the Gas Act (1986) and that civil action may be taken. In some cases a criminal act may have occurred, in which case liaison with the Crown Prosecution Service (CPS) may be necessary.
77. As under the NRPS proposal being developed by the Gas Forum, we recognise some Suppliers will want to procure debt collection and litigation services centrally therefore propose that the CRPU be obligated to offer these services to any Supplier who wishes to procure it from them. As with the other Optional services in this proposal however, the terms upon which any service would be provided would be for the CRPU and the contracting Supplier to agree on a bi-lateral basis.

### **Ongoing Monitoring of Sites**

78. We believe that where a customer has shown both the ability and the willingness to steal gas, the risk of further offences at that site is higher than the average risk posed by the population at large. To that extent, and at least in the time immediately following the detection, our experience is that there is merit in Revenue Protection Service providers completing future visits to the site to ensure that they have not re-offended.

79. We consider that as part of their obligation to offer field services to those Suppliers who request it, the CRPU should also offer to monitor sites where theft has been detected to Suppliers who request it. For clarity, this is considered to be a separate service line for the CRPU and need not only be provided to those Suppliers who contract for field services from the CRPU.
80. As with all other Optional services in this proposal, the CRPU and the contracting Supplier will have full flexibility over how this service is to be provided, including over the number and the frequency of visits. This will enable Suppliers to procure a service which best suits their situation, notwithstanding the fact that the SETS will incentivise them to ensure that the provisions they procure genuinely detect the theft on their portfolio.

### **Settlement Services**

81. Suppliers have an obligation to report details of any theft detected through to the relevant Network Owner<sup>13</sup> who is then obligated to treat the energy assessed to have been stolen as if it had not been used for the purposes of settlement<sup>14</sup>, instead allowing the costs associated with it to be socialised through the Reconciliation by Different (RbD) process.
82. We are aware that there are those who argue that this mechanism perpetuates a misallocation of energy in the market and that it must therefore be amended as part of any theft reform package. Having considered the alternatives however, we have decided against proposing any reform in this area.
83. Specifically, we have considered models which socialise all stolen energy and any revenue collected through to models which assign all stolen energy costs and revenue to the registered Shipper, but have found that each of these models has significant issues with them.
84. As we have argued above, the current socialisation of the costs of theft creates a situation where the majority of Suppliers will not deal appropriately with the theft which occurs on their portfolio, as the costs associated with that Revenue Protection activity outweigh any savings they receive following a theft detection. We consider that this disincentive to act is mitigated in this proposal by the inclusion of the SETS incentive scheme, and thus is no longer a problem which necessarily requires addressing.
85. We acknowledge the arguments of some that it is intrinsically unfair to socialise the costs of theft across the market and that the Registered Supplier of the customer guilty of an offence should instead meet the cost as they would do with usage under normal circumstances, but we argue that

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<sup>13</sup> Standard Condition 17.3 of the Supply Licence.

<sup>14</sup> Licence Condition 7 of the Transporter's Licence.

this would create a new and significant disincentive on Suppliers to act. Specifically, given that our experience is that Suppliers are only able to collect approximately 25% of the revenue associated with theft, the assignment of 100% of the costs would significantly increase the disincentive on those Suppliers to find theft.

86. Even if this had the desirable effect of creating an incentive on Suppliers to pursue the customer for the lost revenue, we believe it is implausible to believe that this would lead to 100% of all revenue being collected, particularly in the domestic market where consumer protection regulations limit the Supplier's ability to recover the revenue lost during theft. To the extent that the amount of revenue collected will always be less than the amount of settlement costs a Supplier would face under this model, a disincentive would always exist.
87. We consider this impact may be mitigated by a similarly significant increase in the value of the SETS incentive scheme but believe that the level of increase required in this scenario would be so large as to make the scheme disproportionate in its effects, even if an assumption was made that revenue collection performance improved to 50% or more.
88. We also acknowledge the argument some make that if settlement costs cannot be allocated to the Registered Supplier without unintended consequences then the revenue collected from customers following a theft detection must also be socialised. Again, we have considered the adoption of this settlements model in this proposal but have rejected it for the fact we consider it is likely to create a significant disincentive on Suppliers to pursue the customer for the lost revenue. If, for example, a Supplier with a 5% market share of Supply Points knew they would only keep £0.05 for every £1.00 they collected from a customer, we believe that they would be incentivised to limit the amount of money, time and resource they spent in collecting the amount owing. This would actually lead to an increase in the amount of theft which the general customer population would have to fund and reduce the deterrent against committing theft which full revenue recovery creates.
89. We are aware that some are proposing that these disincentives to act, either in detecting theft in the case of the former model or the disincentive to collect revenue in the case of the latter model, can be fully addressed by some assurance regime which scrutinises Supplier debt collection performance. Notwithstanding the fact that neither this process nor the remedies that underpin it are adequately defined at the time this proposal was being drafted, we consider that the nature of both detecting theft and collecting the associated revenue from customers make it relatively easy to comply with an obligation to act and yet still not carry out the activities to the same standard as would be achieved if Suppliers had a financial interest in the results. Our conclusion is that both the detection of theft and the collection of revenue need to be incentivised, and that as such the only appropriate settlement model is the current one.

90. We accept however that the current settlements process fails to accurately ensure that, following a theft detection, the Annual Quantity (AQ) for the given site is corrected such that it as accurately as possible reflects the actual gas usage at the site. Currently, the AQ is corrected over time as new meter readings are collected, potentially misallocating industry costs in the intervening period. We therefore propose that, as part of this proposal, Suppliers are obligated to correct the AQ following any theft detection using the existing BTU process where it is available<sup>15</sup>.
91. We also recognise that those Suppliers taking services from the CRPU may also find it efficient to also commission the CRPU to submit the necessary information regarding theft detections, including an assessment of the amount of gas stolen and any BTU forms which may be required, to the Network Owner for settlement purposes. To this extent, this proposal will obligate the CRPU to offer this administration service to those Suppliers who wish to contract for it.
92. For clarity, as the use of the BTU process would be a new obligation on Suppliers, any party not contracting with the CRPU for this aspect of the service would need to make alternative provisions or risk the prospect of regulatory action.

## **Other**

93. The key principle behind Proposal Two is that Suppliers should retain overall accountability for detecting the theft on their portfolio but that they can choose to discharge that accountability themselves, through the CRPU or any other body they so wish. We argue that the inclusion of incentives in this proposal means that Suppliers will have a financial interest in seeing the best possible outcome and that this in turn will drive results.
94. To this end we consider it entirely likely that Suppliers will want to procure new Optional services which we have not envisaged in this proposal which increase the volume of theft they detect or reduce the cost associated with that detection activity. We therefore propose that the CRPU should also have an obligation to reasonably consider, and if necessary, facilitate on a commercial basis any new service which a Supplier or Suppliers may wish to commercially procure, provided it is consistent with the CRPU's primary objectives.
95. This would not be an obligation on the CRPU to provide all services which a Supplier wishes, nor indeed would Suppliers be obligated to take any new service from the CRPU. Instead, we propose that Suppliers may procure new services from whichever provider they like, including the CRPU. To ensure transparency and fairness however, we intend that the CRPU would

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<sup>15</sup> Currently, the BTU process is only offered by large Transporters. It is a mechanism where the AQ may be manually altered following the receipt of new evidence which demonstrates its inaccuracy.

also be obligated to be transparent about any bi-lateral services it is now offering and be willing to provide that service on the same basis to any other Supplier who wishes to take it, on a non-discriminatory basis.

## **GOVERNANCE**

96. These Proposals therefore have four elements; the Co-ordination service element through the RPACA, the Optional service element through the CRPU, the Supplier Energy Theft Scheme (SETS) element and the Code of Practice element. Suppliers will be incentivised to detect theft through the SETS, the RPACA will co-ordinate and facilitate that activity with, the CRPU will provide them with a means through which to do that and the Code of Practice will set out precisely how that activity should be carried out, standardising customer treatments in the process. The audit provisions within the SETS proposal assess compliance with both the Gas Act and Code of Practice provision, giving the entire proposal assurance. Each of these elements requires governance arrangements to ensure they operate effectively.

## **SETS**

97. The SETS scheme set out in Uniform Network Code (UNC) Modification Proposals 0277 and 0346 proposes that the incentive be placed on Shippers through the UNC itself, with the intention that they will then pass this cost or benefit through to their registered Supplier. It is our proposal that the rules for the operation of this Scheme remain in the UNC and be subject to all the governance rules which that contains.

98. For clarity, it is immaterial for the purposes of SETS over the route a Supplier uses for managing theft on their portfolio. If a Supplier opts to use the CRPU as the delivery mechanism for their revenue protection work then they will still be subject to the incentive mechanism; SETS is simply used as the mechanism to encourage Suppliers to manage the theft which exists on their portfolio in the most effective way they deem fit.

## **CoP**

99. The Code of Practice sets out both obligations on Suppliers in respect of the steps they must take once they have made a detection and what are considered to be industry best practice or guidance on how theft may be both detected and handled post-detection. Our proposal is that once developed, specific gas and electricity Code of Practice documents are placed in to the Supply Point Administration Agreement (SPAA) and the Distribution Connection Use of System Agreement (DCUSA) respectively so that they become binding on Suppliers.

100. Any Supplier found to be in breach of the provisions in Code would be in breach of their obligations under either SPAA or DCUSA and face potential remedies under those Codes. We envisage that such breaches will become

apparent during the audit provision contained with the SETS proposal. For clarity, under this proposal Suppliers will remain responsible for the actions of their agents, including the CRPU.

101. We acknowledge that some Suppliers are not party to the SPAA and that these governance arrangements may therefore cover, an albeit large, part of the market. We therefore argue that in considering this proposal Ofgem should seek to change the Gas Supply Licence such that all non-domestic Suppliers are obligated to become signatories to the SPAA. Was this not to be possible a mechanism must be found to enable these Suppliers to be obligated by their contents without acceding to the wider agreement. We can point to precedents where this arrangement works, for example the way in which non-domestic Suppliers adhere to the Review of Gas Metering Arrangements (RGMA) provisions in SPAA and believe a similar arrangement could be put in place for the Code of Practice. Alternatively, we consider a UNC Modification Proposal may be necessary to obligate all Shippers to ensure that their Suppliers comply with the provisions of the SPAA Code of Practice.

## **RPACA and CRPU**

102. We acknowledge that neither the RPACA nor CRPU will be party to an industry Code and that as such the obligations which bring them in to being, dictate what services they offer and set out how it will carry out its duties will need to sit on Suppliers themselves, and then be backed off in the commercial contract between the industry and the RPACA and CRPU.

103. We consider that the creation of a new industry code and related governance arrangements to achieve this would unnecessarily increase the implementation timeline for this proposal without adding much benefit. We therefore propose that a new schedule is created in the SPAA which obligates Suppliers to procure the services set out in either Proposal One or Proposal Two of this document. It is our opinion that the Articles of Association for SPAA Ltd allow for it to become a contracting vehicle<sup>16</sup> and that as such it is entirely appropriate for SPAA Ltd to manage the procurement exercise and then take on the role of managing the contract between SPAA Ltd, on behalf of gas Suppliers, and either the RPACA under Proposal One or the RPACA and the CRPU under Proposal Two.

104. As we argue above, we recognise that not all non-domestic Suppliers are party to the SPAA and that as such a solution must be found so that they too have access to, and help fund, the Co-ordination services of the RPACA. We consider that this could either take the form of a new obligation on these Suppliers to become parties to SPAA or the ability of these parties to adhere to the new schedule in the same way as they currently do with the Review of Gas Metering Arrangements (RGMA) provisions. For clarity, we do not

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<sup>16</sup> The Supply Point Administration Agreement, Schedule 4.



foresee any governance issues with the provision of Optional services under Proposal Two to non-SPAA parties as the funding for these services will be on a bi-laterally negotiated price (see below).

105. Any new services provided by the CRPU as described in paragraphs 93 to 95 will be deemed to be “non-code” services and not require inclusion in either the contract between SPAA Ltd and Suppliers. Neither will they require a change to be completed against the relevant SPAA Schedule. This will ensure that the CRPU is able to innovate and develop quickly, without relying on an industry change process to adapt and evolve. To that end, the services specified in this proposal are intended to be only the bare, regulated, minimum that the CRPU will provide.

## **FUNDING**

106. The funding of any services offered under either of these proposals will be divided in to two distinct areas, the funding required for the Co-ordination services under Proposals One and Two and the funding for the Optional and future services considered under Proposal Two only.
107. The Co-ordination services contemplated under under Proposals One and Two will incur cost for the RPACA largely in proportion to the prevalence of theft on a Supplier’s portfolio rather than the volume of gas stolen on any portfolio. We therefore propose that Co-ordination services will be funded by all Suppliers based on their market share of Supply Points. We have considered funding mechanisms which involve Suppliers funding the RPACA based on the amount of theft Suppliers subsequently find on their portfolio, with those who have more theft on their portfolio paying more on the basis that they drive more cost in to the RPACA operation. We considered that this created a disincentive on Suppliers to co-operate with the RPACA however and have therefore discounted it.
108. Optional and future services detailed in Proposal Two will be paid for by those Suppliers who take them based on the price which is negotiated with the CRPU. As under the third primary objective of the CRPU, they will have an obligation to provide services in a way which does not unduly discriminate between the Suppliers to whom the services are provided to. The CRPU will therefore be required to ensure that the cost of identical services provided to different Suppliers will be the same, with any differential in services leading to a proportional differential in cost.
109. This approach ensures that Suppliers have complete flexibility in procuring a service which meets the specific needs of their portfolio, maximising value for money for customers in the process. This will also allow Suppliers and the CRPU sufficient flexibility with which to innovate in approach at any stage. We consider that the existence of the SETS will be sufficient to ensure Suppliers do not simply choose the “lowest cost option” but instead to seek options which lead to the detection of theft at the best value.

## COST

110. There are four elements of cost to consider in relation to this proposal, specifically the cost associated with the SETS, with the Code of Practice, the provision of Co-ordination services by the RPACA and the provision of optional services by the CRPU.
111. The cost of implementing the SETS was detailed in UNC Modification Proposals 0277 and 0346 by the Network Owners' agent, xoserve. During the development of those proposals, they identified that the industry processes required to support the SETS would cost no more than £380k to build and no more than £130k to cover both the ongoing management of those processes and annual audit of the scheme.
112. The Code of Practice itself has no cost associated with it, although we acknowledge that any Supplier not currently compliant with the obligations within it may incur a nominal cost associated with changing their working practices and processes. As no Supplier has accepted that they are not compliant with these provisions we have assumed no net cost for this element of the proposal.
113. There will be a cost associated with the provision of Co-ordination services through the RPACA under Proposal One and Two, although we consider these to be comparatively low, particularly if the Network Owners or their agent, xoserve, take on this role. For example, xoserve's Conquest system already provides Suppliers with the mechanisms to provide the management information contemplated by this proposal.
114. We also note that they also provide and resource the for the telephone service through which gas emergencies are reported<sup>17</sup>, and believe that this telephone service could also be advertised as the number to use to report suspicions of theft. Any increase in cost would therefore be limited to an increase in resource associated with managing the increase in use of these two processes. Similarly we believe that the costs associated with providing Co-ordination services such as change of supply co-ordination would be substantially less if the Network Owners were to provide them, considering their existing role in managing that process.
115. Finally, we do not consider that the cost of either maintaining a stolen meters register, co-ordinating the industries efforts with other external agencies or providing a forum where best practice can be shared will have onerous costs, instead constituting primarily of resource provision.
116. We consider that the costs associated with the Optional services considered in Proposal Two will be greater however. Our own experience is that activities such as data collection, lead generation and field services in

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<sup>17</sup> 0800 111999

particular all have greater costs associated with them, but believe that by structuring this proposal so that the provision of these services is done through the competitive market costs can be driven to a minimum. We consider for example that the CRPU will be able to compete against other service providers in the existing market, enabling Suppliers to choose whichever provider offers them, and customers, best value for money. As a guide, in UNC Modifications 0277 and 0346, we argued that, based on our own experience of providing Revenue Protection services, the total industry cost of Optional services such as those detailed in Proposal Two would be approximately £10.062m<sup>18</sup>.

117. We, as part of the Gas Forum, have also procured cost estimates for these services as part of the development of the NRPS proposal, and as the specification of each service is broadly the same, we believe they also will provide an accurate cost estimate for this proposal. An estimate of these costs will be published separately, in advance of the Theft Impact Assessment, by the Gas Forum.
118. We argue that as the CRPU as proposed in Proposal Two will be operating in a competitive market, and not as an un-regulated monopoly service provider as proposed elsewhere, the expectation is that year on year, either the costs of providing these services will fall or the quality of service provided will increase; improving the value for money customers receive. Furthermore, we argue that as our proposal allows Suppliers the autonomy to procure the service which best suits them means that bespoke solutions providing best value for money can be found across the industry, with the existence of SETS ensuring that Suppliers remain focused on delivering results.

## **KPIS / SLAS**

119. There will be no Key Performance Indicators (KPIs) or Service Level Agreements (SLAs) for the Co-ordination services specified in Proposal One and Two other than the KPIs and SLAs set out above in the detailed description of each service.
120. KPIs and SLAs associated with the Optional and future services set out in Proposal Two will be negotiated on a bi-lateral basis between the CRPU and the contracting Supplier. This will enable the Supplier in question to procure a service which meets their specific needs. Again, we argue that the existence of the SETS will ensure that Suppliers are focused on agreeing arrangements which deliver results.

## **INTERACTION WITH SETS**

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<sup>18</sup> UNC Modification Proposal 0277, page 4, "The Value of the Scheme"

121. The Supplier Energy Theft Scheme was set out in UNC Modification Proposals 0277 and 0346. This scheme stipulates that Suppliers are obligated to pay in to a fund an amount proportionate to their market share of either Supply Points or aggregate NDM Annual Quantity (AQ) and then take money out of the fund based on their share of either total thefts detected or their share of total theft volumes detected. The effect is that those Suppliers who perform better than their relative size suggests will be rewarded and those whose performance is worse than their relative size suggests will be penalised. This creates an incentive on Suppliers to detect theft.
122. Our proposal is that the SETS, as set out in either of these UNC Modification Proposals, is implemented alongside either the RPACA under Proposal One or the RPACA and CRPU under Proposal Two so that Suppliers are incentivised to find theft, regardless of the mechanisms they choose to use to detect that theft.
123. We recognise that if more than one Supplier contracts with the CRPU under Proposal Two for the provision of field services however, it may be appropriate for those Suppliers to receive aggregate incentive payments from the scheme, rather than to receive incentive payments based on the amount of theft the CRPU has found for those Suppliers. This would avoid the potential issue which may arise when different Suppliers receive different levels of performance from the CRPU and are then financially penalised for that, but it may be argued it would also dilute the incentives Suppliers face if they felt that other parties contracted to the CRPU were substantial efforts to co-operate with the CRPU.
124. We have not stated a preference within this Proposal on this issue, but have set out both implementation options for consideration. For clarity, under either implementation option under Proposal Two, contracting Suppliers will still be required to pay in to the Scheme based on their relative market share of either Supply Points or aggregate NDM AQ.

## **ASSURANCE**

125. There will no formal assurance process other than the audit mechanism set out in UNC Modification Proposal 0277 and 0346 in relation to the SETS. This provided for an annual audit of Supplier actions in the course of detecting theft, including an assessment of whether they have complied with both the Gas Act (1986) and any relevant Code of Practice in force at that particular time. Any failures which the audit identifies are publicised so that breach proceedings may, if appropriate, be progressed, and financial penalties will applied in the form of SETS payments being deducted.
126. Our proposal is that any Supplier contracting with the CRPU under Proposal Two for field services will be responsible for the actions of their agent, and therefore bear the risk associated with any breach of the regulations. To this end, the actions of the CRPU, and the extent to which it complies with the

legislation and regulation in this area will be the direct responsibility of the Suppliers who contract with it.

## **IMPLEMENTATION TIMELINE**

127. An indicative implementation timeline is attached to this Proposal as Appendix One. Within Proposal One we outlined two distinct delivery options; the first where the Network Owners or their agent, xoserve, were tasked with the provision of Co-ordination services, and a second where a service provider was selected following a competitive tender. The timeline for delivery of either option is detailed in Appendix One.
128. Were the first implementation option to be taken, we estimate that this proposal would start delivering benefits early in Q4 2011 through the SETS, with Co-ordination services provided through the RPACA potentially being provided by the end of Q2 2012. This assumes an Ofgem decision on theft reform is made by the end of September 2011.
129. Importantly all of the Co-ordination services we propose in this document are not already provided, and could not be effectively provided, by the competitive market, meaning an Ofgem direction to implement could easily be made. We consider that this is not the case for the proposal being developed under the Gas Forum which seeks to monopolise an existing competitive market in order to provide services which could equally be delivered through an effective competitive market. We believe that a direction to implement the model developed under the Gas Forum may therefore be in conflict with Ofgem's primary duty and thus require Ministerial approval, potentially extending the delivery timeline considerably.

## **BENEFITS**

### **Impact on theft detected**

130. In our consultation response to UNC Modification Proposals 0277 and 0346 we argued that if the SETS was implemented, every Shipper would be incentivised to detect theft as we have done. The responses to the recent Ofgem Theft Questionnaire also highlighted that the best performing Supplier was able to detect theft on approximately 0.0263% of its portfolio. Therefore, if every Supplier was suitably incentivised to tackle theft, as we propose under SETS, and therefore raised their performance to this benchmark, a total of 5917 cases of theft would be detected. This would be an increase of over 3000 theft detections per annum.
131. However we argue that this is the absolute minimum improvement which can be expected, and believe that the increase in the effectiveness of the competitive Revenue Protection market will not only drive down the marginal cost of detecting theft, but will also drive future improvement and innovation. This in turn will have a positive impact on the amount of theft detected, year on year.

132. Additionally, we consider that the provision of Co-ordination services set out in both Proposal One and Proposal Two in this document will enable more theft to be detected, through improved visibility of both where and how theft is happening and the co-ordination of best practice and multi-agency efforts. Our conclusion therefore is that 5917 theft detections per year is merely the absolute minimum benchmark for Year One and that in reality we expect this proposal to lead to a far more material increase in theft detection levels. Indeed, we believe the potential effect of competition to be so material that we envisage a 50% improvement in minimum theft detection rates provided above, year on year.

### **Impact on other Key Performance Indicators**

133. In addition to the detection of more theft of gas, this proposal will lead to a number of other, ancillary benefits. In particular, and as a direct consequence of Suppliers engaging in more theft detection activity, from data analysis to theft detection and revenue recovery as a result of the introduction of incentives, there will be an increase in the number of

- a. Leads generated,
- b. Sites visited,
- c. Non-theft related outcomes identified, for example faulty meters and Shipperless or Unregistered sites,
- d. Detections of theft in the course of conveyance, otherwise known as theft from the Network, and
- e. Revenue recovered, and therefore a reduction in the amount of gas reconciled through the Reconciliation by Difference (RbD) mechanism.

134. There is no reliable industry management information relating to the current level of performance in some of these areas, and therefore it is difficult to quantify the precise level of incremental benefit this proposal will have in terms of, for example, the increased number of Shipperless sites or faulty meters which will be identified.

135. Following the recent Ofgem Theft Questionnaire however, Ofgem have published data which shows that if every Supplier raised their performance to meet the current benchmark in terms of the number of sites they visited, 17177 properties would be inspected each year. As with the volume of theft detected under this proposal, we consider that the existence of the SETS, the effect of innovation brought about by the existence of a competitive market and the benefit derived from the provision of Co-ordination services, would mean that this is the absolute bare minimum performance that would be delivered by this proposal, and that year on year improvements could be expected.

136. We argue that the results of the remaining Key Performance Indicators listed above would be a direct function of the number of sites visited, with an increase in site inspections leading to a proportional increase in the number of Shipperless or Unregistered sites identified, increase in the amount of faulty meters or theft in the course of conveyance detected, and an increase in the amount of revenue recovered

### **Cost Allocation**

137. At the moment, the costs associated with theft are socialised across the entire Small Supply Point (SSP) sector, regardless of where that theft originated or which Shipper's inaction led to it. By ensuring that those who present the biggest risk of generating unidentified gas costs from inaction in resolving theft bear the biggest risk and those who effectively manage their risk are rewarded, through the SETS incentive payments and penalties system, costs will be reallocated in a more equitable way, thus facilitating an improvement in Shipper's and Supplier's ability to compete fairly. This will be done in "*a transparent and easy to understand*" way<sup>19</sup>.

### **Short Implementation Time**

138. Unlike the NRPS proposal being created under the Gas Forum, this proposal would be ready to deliver benefits early during Quarter 4 2011, assuming an Ofgem decision to implement it comes before September. xoserve confirmed during the development of UNC Modifications 0277 and 0346 that SETS could be operational immediately following an Ofgem direction to implement it, providing Suppliers with an imperative to detect theft by linking their financial returns to theft detection performance. We also consider that, whilst a tender process would need to be undertaken for Optional services such as the data collection, lead generation and field services, the Co-ordination services detailed in this proposal are such that the Network Owners or their agent, xoserve, could undertake them, on a User Pays basis, at relatively short notice.
139. We also note that as CRPU envisioned by Proposal Two is not a monopoly service provider but another player in a wide, more effective competitive market, the steps required to bring it in to being are likely to be less onerous. We consider that any Ofgem decision to implement an RPACA under both Proposal One and Proposal Two will not require Ministerial or European approval as the Co-ordination services provided by it are not already provided, and could not be effectively provided, by the existing competitive market. We consider this avoids a conflict with Ofgem's duty to "*protect the interests of consumers, where possible by promoting competition*". We note that this is not necessarily the case for the NRPS proposal being developed

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<sup>19</sup> ENA / ERA "Report of the Theft of Energy Working Groups", page 67.

under the Gas Forum, and thus argue that our proposal can be delivered much more quickly.

### **Ancillary Benefits**

140. We also consider the administration costs of this proposal are not onerous. In relation to SETS, the data required in order to make the scheme operate is already known and the cost of developing the supporting industry processes would cost no more than £380k, with a further £50k per annum to support and maintain those processes<sup>20</sup>.
141. We also consider that as the industry processes which would support the provision of the Co-ordination services detailed in both Proposal One and Proposal Two are already in existence, the cost associated with this element could be easily minimised by requiring the Network Owners or their agent to fulfil them on a User Pays basis. We recognise that the costs associated with some of the Optional services provided by the CRPU under Proposal Two may be more onerous, but as they replace the investment Suppliers themselves make in Revenue Protection activity we believe that the net cost to the consumer will be low.
142. We also consider that the governance of the scheme is relatively easy to create and manage; the SETS will be managed by the Network Owner's agent under the UNC, the Code of Practice will be managed by Suppliers themselves under the SPAA and the DCUSA with the RPACA and CRPU elements of these proposals also forming part of an existing governance regime.

### **Facilitation of SPAA Relevant Objectives**

143. Although this proposal has not been raised under any formal Code governance we have provided an assessment of the benefits of this proposal against the SPAA relevant objectives<sup>21</sup> for the purposes of demonstrating a benefits case. We consider that this proposal facilitates them as follows.

***“(b) the furtherance of effective competition between Gas Suppliers and between relevant agents;”***

144. This proposal will provide Shippers with both the commercial incentive to detect theft on their portfolio and the means with which do it. In a competitive environment such as the energy supply market the potential costs, being calculated at a sufficient level to provide for an adequate

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<sup>20</sup> As per the xoserve costs provided in the Rough Order of Magnitude for Modification Proposals 0277 and 0346.

<sup>21</sup> As set out in Standard Licence Condition 30.6 of the Supply Licence.



Revenue Protection service (see above), will make it commercially important to detect the theft on their portfolio, with benefits payable for results only.

145. Furthermore, the creation of a central body to co-ordinate efforts across the industry and share best practice will enable further increases in the volume of theft detected. Finally, we consider that by aiding the element of competition in the provision of Revenue Protection services, the industry as a whole will be incentivised to continually innovate and improve, driving down the marginal cost of detecting theft and driving up the volumes of theft found. The consequence of this modification therefore will be an increase in the amount of theft detected by Suppliers.
146. By reducing theft and correcting the apportionment of misallocated energy, costs should be correctly apportioned across those who drive costs into the market, therefore improving competition. Currently the costs of theft in the market are borne solely by SSP suppliers based on their market share. This is inequitable and disadvantages those shippers in the SSP market who invest in resolving theft on their portfolio. By ensuring that the costs associated with theft are assigned to those Shippers who perform poorly in terms of theft detection, thus driving costs in to the market, costs will be more fairly assigned, and competition between shippers and Suppliers will be improved.

## **RECOMMENDATION**

147. Our proposal, with the SETS, delivers all the advantages of the NRPS model developed under the Gas Forum without any of the disadvantages. We therefore recommend that following the forthcoming Theft Impact Assessment, Ofgem direct the implementation of either UNC Modification Proposal 0277 or 0346 followed as soon as possible by a direction to implement either the RPACA on its own under Proposal One or both the RPACA and the CRPU under Proposal Two. We also recommend that these should both be complemented with the DCUSA and the SPAA Code of Practice currently being developed.
148. Our preference is that the SETS detailed within UNC Modification Proposal 0346 is used for this purpose as we believe it more effectively incentivises theft detection in the non-domestic sector, where the risk of theft is greater due to the potentially larger volumes of gas stolen. We recognise some may argue that the full evidence required to support our assertions will only come once the Allocation of Unidentified Gas Expert (AUGE) publishes their initial methodology and have therefore also proposed Modification Proposal 0277 which allocates incentive payments and charges on a market share of Supply Point basis; ensuring that Suppliers are incentivised to invest a sufficient amount of money to provide theft detection coverage for their size of portfolio. Although we have a preference for Modification Proposal 0346 for the reasons given above, we believe that both proposals would provide real and lasting reform to the way in which theft is detected in the UK gas market.