



Promoting choice and value

for all gas and electricity customers

Tackling gas theft

Consultation

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Overview:

Theft of gas has a material impact on customers in terms of cost and safety. Ofgem considers that the existing regulatory framework does not adequately encourage suppliers to be proactive in detecting theft. In this document we are requesting views on proposed new supply licence obligations to strengthen the arrangements for tackling theft. We are also consulting on three specific industry proposals to improve theft detection.

Context

This document reflects the commitment set out in Ofgem's Corporate Strategy and Plan 2010-15, to support industry initiatives to introduce revised theft arrangements and consider whether further action is required.

The focus of this document is on the gas market. We aim to bring forward proposals for reform in the electricity market, where necessary, in spring 2012.

Our proposals also support several key themes outlined in the Ofgem's Corporate Strategy and Plan 2011-16. These include; promoting value for customers and protecting the interests of vulnerable customers, helping to maintain security of supply and contributing to the achievement of a low carbon economy.

Associated documents

- Theft of Gas and Electricity - Discussion Document, April 2004. Ofgem (Ref: 85/04)
<http://www.ofgem.gov.uk/Markets/RetMkts/Compl/Theft/Documents1/6839-8504Energytheft.pdf>
- Theft of Gas and Electricity - Next Steps, January 2005. Ofgem (Ref: 06/05)
http://www.ofgem.gov.uk/Markets/RetMkts/Compl/Theft/Documents1/9342-next_steps.pdf
- Report of the Theft of Energy Incentive Group – Final Proposals, June 2007. ENA and ERA.
<http://www.energy-retail.org.uk/documents/ReportoftheTheftIncentiveSchemeDevelopmentGroup-FinalProposalsJune2007.pdf>
- Report of the Theft of Energy Work Group, April 2006. ENA and ERA.
<http://www.energy-retail.org.uk/papers/ElectricityandGasReportFinalVersionpdf.pdf>
- UNC277 - Creation of Incentives for the Detection of Theft of Gas (Supplier Energy Theft Scheme), Final Modification Report, 21 January 2011.
<http://www.gasgovernance.co.uk/0277>
- UNC346 - An Alternative to the Supplier Energy Theft Scheme Based on Throughput, Final Modification Report, 21 January 2011.
<http://www.gasgovernance.co.uk/0346>
- The Creation of a Revenue Protection Activity Co-ordination Agent (RPACA) and a Central Revenue Protection Unit (CRPU), 8 April 2011. British Gas
<http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=67&refer=Markets/RetMkts/Compl/Theft>
- NRPS Workgroup Report to Ofgem, 16 June 2011. Gas Forum
<http://www.gasforum.co.uk/admin/documents/GF%20NRPS%20Final%20Report%20v1.0.pdf>

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Executive Summary

Among the 22.5 million gas customers in Great Britain, some will seek to avoid paying for the gas they consume. Theft of gas increases the costs paid by customers and can have serious safety consequences. It also leads to a misallocation of costs among suppliers, which can distort competition and the efficient functioning of the market.

Ofgem is keen to see action taken to reduce the amount of gas theft. We do not consider that the current regulatory arrangements – or the actions taken by industry participants within that framework – necessarily act in the best interests of consumers. The incentives for suppliers to detect theft proactively are, in some cases, weak.

In this context, we propose to make changes to the regulatory framework for tackling gas theft. We also propose to add impetus to the process of industry-led reform, to ensure that recent industry work translates into positive action.

In terms of direct action, we propose to align the requirements between gas and electricity by introducing a new obligation on gas suppliers to detect and prevent theft. Our proposals would also require suppliers to investigate suspected theft and do so in accordance with minimum standards set out in the licence.

In response to our call for action, the industry has developed three specific schemes designed to increase theft detection from current levels. These include proposals to: pool industry data and resources to identify sites with the highest risk of theft; improve incentives for suppliers to detect theft; and to provide services to the market to help suppliers detect and investigate theft. We welcome these proposals and will decide which, if any, should be implemented.

Our initial assessment of these proposals is set out in a draft Impact Assessment, which is published alongside this document. Our analysis suggests that each of the three proposals would help reduce the incidence of gas theft, and would have consequential benefits for customers and the market more widely. We welcome views on our analysis and on which of the proposed schemes would be most effective and proportionate for tackling gas theft.

We are seeking responses to the consultation questions set out in this document – and any other comments – by 26 October 2011. In the light of this feedback, we aim to respond by the end of 2011 with our decision on how to take forward the proposed licence amendments, and which, if any, of the industry proposals should be implemented.

1. Introduction

Chapter Summary

In this chapter we describe the impact of theft and the relevant aspects of the current regulatory framework. We describe our role in delivering appropriate arrangements. We then summarise previous work on gas theft, associated developments in electricity and other related work areas.

Definition

1.1. For the purposes of this consultation we have used the term "theft" as a simple way to describe a number of offences under schedule 2B of the Gas Act 1986 where a customer prevents a meter from correctly registering the amount of gas supplied, has damaged equipment or reconnects the supply without the relevant permission¹. Where relevant, we have also set out where we consider that our proposals may have other applications, for example in identifying and tackling other sources of unrecorded gas consumption such as faulty metering.

Materiality

1.2. Theft of gas has safety implications for customers that commit or commission the offence as well as other individuals in close proximity, industry staff that work with the physical gas infrastructure as well as the emergency services.

1.3. Evidence provided by one supplier on gas theft incidents in 2010 made a direct link to two fatalities and 36 injuries to customers, of which two were considered to be serious.

1.4. Improved arrangements to detect and prevent theft (including where a customer is deterred from committing an offence) are therefore expected to improve safety on the gas networks.

¹ Schedule 2B, paragraph 10 of the Gas Act 1986 establishes that it is an offence to intentionally, or by culpable negligence interfere with the index for registering consumption on a meter, prevent a meter from correctly recording consumption or damage gas fittings provided by the transporter or the supplier or a service pipe provided by the gas transporter. Paragraph 11 establishes that it is an offence to restore a disconnected supply without the relevant consent from a supplier or gas transporter.

1.5. Theft of gas also has cost implications for customers. Estimates of the retail value of stolen energy range widely from £64m to £220m per year². This equates to between £2.70 and £9.80 per gas household per year³.

1.6. Gas theft also impacts on suppliers. Suppliers will, for example, incur costs in tackling theft incidents, lose revenues and their employees and agents will be subject to safety risk. Networks can also be impacted for example, through loss of supply caused by leaks and explosions as well as damage to infrastructure.

Role of Ofgem

1.7. In this context, we consider that Ofgem's role is to facilitate the development of effective arrangements to tackle energy theft. This is consistent with our principal objective to protect the interests of current and future gas and electricity consumers and our duties, for example in relation to safety. The tools that we intend to use to deliver this requirement are the following:

- Propose licence conditions, where necessary, to establish the broad regulatory framework
- Enforce existing and new licence requirements
- Fulfil our responsibility to consider modifications to industry codes and approve these where we consider that they will deliver benefits
- Continue to work with the industry to develop and refine proposals to improve the gas theft arrangements.

Current regulatory framework

Suppliers

1.8. Suppliers are required by their licences to conduct two-yearly meter inspections. This includes an inspection of the meter and associated equipment for evidence of theft.

1.9. Once a supplier suspects that a gas theft may be occurring, it is required by its licence to inform the relevant gas transporter and provide any additional information reasonably requested, including an estimate of any amount illegally taken.

² The figure of £64m reflects the value attributed to gas theft under the gas price control shrinkage incentive mechanism. Of this £60m is allocated to gas theft downstream of the Emergency Control Valve (ECV) and is considered to be the responsibility of suppliers. The estimate of £220m has been provided by British Gas based on its view of the market.

³ These costs have historically been borne by Smaller Supply Points (SSP) which includes most domestic premises and small businesses. Recent changes to the settlement rules, which are explained later in this chapter, will relocate some of these costs to Larger Supply Points (LSPs).

Transporters

1.10. Where theft in conveyance⁴ is detected or suspected, the relevant gas transporter must investigate. Where theft is detected it is then required to use reasonable endeavours to recover the value of the gas from the customer. Under the conditions of its licence, a gas transporter is not required to be proactive in detecting gas theft.

Incentives

1.11. Where a theft remains undetected, the cost of the gas illegally taken and its transportation would not be recovered from the customer. These costs are likely to increase the costs of gas paid by all customers.

1.12. In the Smaller Supply Point⁵ (SSP) market, the extent to which the offending customer's supplier would be liable (via its shipper⁶) for gas illegally taken and its transportation would depend on whether the Annual Quantity⁷ (AQ) associated with that site has reduced.

1.13. If the AQ has not reduced then the customer's supplier would remain liable for the gas and transportation charges. If the AQ had reduced then these charges would be smeared across all shippers in the SSP market⁸. There is a time lag in amending AQs and therefore the customer's supplier is likely to bear at least some of these costs.

1.14. In the Larger Supply Point⁹ (LSP) market, individual meter point reconciliation means that an LSP shipper is likely to pay gas and transportation charges based on metered consumption. Where stolen gas is not metered (or an adjustment is not subsequently made to account for it once detected) the cost of stolen gas has

⁴ Gas transporters are required under SLC 7(1) and (2) of their licences to investigate theft in conveyance. Under SLC7(11) a supply taken upstream of the ECV is generally considered to be in the course of conveyance. See

http://epr.ofgem.gov.uk/document_fetch.php?documentid=14307

⁵ An SSP is a supply point with an annual consumption of less than 73,200kWh (2,500 therms).

⁶ For clarity, unless specifically stated, when we refer to a shipper in this document we are referring to the shipper with a contractual relationship with the supplier whose customer has taken an illegal gas supply. We assume that there is an exclusive contractual relationship between the shipper and the supplier and pass through of costs related to the theft from the shipper to the supplier.

⁷ The AQ is an estimate of the expected consumption at a site during the year based on historic meter reads.

⁸ Arrangements are now in place for the costs of unmetered consumption to be allocated to the LSP market as well as the SSP market. Under these proposals, SSP shippers would still be responsible for the costs of any error in allocation in the SSP market and would also be liable for any error in the allocation arrangements for the LSP market.

⁹ An LSP is a meter point with an annual consumption greater than 73,200kWh (2,500 therms).

historically been borne by the SSP sector. However, recent modifications to the Uniform Network Code (UNC) require shippers in the LSP market to be responsible for these costs. Where a supplier in the LSP sector declares the volume of gas illegally taken to xoserve, their charges¹⁰ would be adjusted and the industry smear would be partially removed. In practice, this declaration does not occur frequently.

1.15. A supplier will seek to recover its other supply costs (eg marketing and billing) from customers. Where this is not done through the standing charge, it is likely to be recovered in proportion with their metered consumption. Where a customer takes an illegal gas supply and consumption is not metered, other customers are likely to bear increased costs to cover the supply overheads.

1.16. Where theft is detected then a supplier may seek to recover charges for gas illegally taken and other costs (such as a meter exchange and theft investigation) from the customer. In some cases, a supplier will be successful in recovering all, or a significant proportion of these charges. However, this is not always the case. Suppliers estimate an average recovery rate of approximately 25% in the SSP market and 60% in the LSP market. We have analysed the cost implications of detecting theft in the SSP and LSP markets. Our results show that, for an average theft with an average rate for recovery of charges, theft detection would have a positive benefit for a supplier in the SSP market however, there is likely to be a disincentive on an LSP shipper from being proactive in detecting a theft. Theft detection is also likely to have a positive impact on reducing customer bills. Further information on our modelling is set out our accompanying draft Impact Assessment.

1.17. Suppliers are eligible for compensation payments from a self-funded scheme where they have identified theft but have failed to recover charges from the customer, having undertaken reasonable endeavours to do so. These compensation arrangements seek to cover elements of the investigation and meter replacement costs as well as transportation costs. In practice, these arrangements are not widely used. A modification proposal has been raised to seek to improve these arrangements and we will consider whether the existing arrangements should be removed, retained or modified as part of this consultation. This is discussed further later in this chapter and in Chapter 4.

Developments to date

1.18. In April 2004, Ofgem consulted on whether the gas and electricity theft arrangements were fit for purpose. In January 2005, we published a follow-up document summarising concerns with the arrangements and welcoming the commitment of the Energy Retail Association (ERA) and the Energy Networks Association (ENA) to establish a workgroup to develop proposals for change.

¹⁰ Other than the capacity element of transportation charges which is based on the AQ.

1.19. In 2006 and 2007, the ERA/ENA workgroup published two reports¹¹. These concluded that gas and electricity market participants do not have the right incentives to deliver optimal behaviour under the current market arrangements. It set out a number of options to improve supplier incentives. It noted that supplier obligations, where they existed, were not well defined and should be reviewed but that this should not be done without addressing the commercial implications.

Gas specific proposals

1.20. In October 2009, British Gas proposed a modification to the UNC¹² (UNC231V) to reduce the disincentives that gas suppliers faced in being proactive in detecting theft. The proposal sought to increase the amount of compensation that a supplier could receive when it had identified a theft but failed to recover its costs from the customer despite using its reasonable endeavours.

1.21. Ofgem consulted on this proposal in December 2010¹³. Responses were broadly positive although some concerns were raised¹⁴. However, it was generally agreed that the arrangements should be considered in light of any further reform proposals in the market. The role of compensation arrangements in the broader context of our theft reforms is discussed further in Chapter 4 of this consultation.

1.22. Review Group UNC245¹⁵ was established in April 2009. It undertook a broad assessment of the arrangements for tackling gas theft. In November 2009, it made a series of recommendations to the UNC Panel. These recommendations included measures to address the lack of incentives on suppliers to tackle theft. It proposed two potential mechanisms, a Supplier Energy Theft Scheme (SETS) and a National Revenue Protection Scheme (NRPS). Both of these proposals have continued to be developed and are the focus of this consultation on improving arrangements for the detection of gas theft.

1.23. In addition, Review Group UNC245 proposed the development of a code of practice on the successful management of gas theft and established initial guiding principles. This code of practice was developed by a joint Distribution Connection and Use of System Agreement (DCUSA) and Supply Point Administration Agreement (SPAA) workgroup. The gas version of the code of practice has now been formally handed to the SPAA so that it can be further developed and brought into that industry code through its change control process.

¹¹ Report of the Theft of Energy Work Group, April 2006 and Report of the Theft of Energy Incentive Group – Final Proposals, June 2007.

¹² UNC231V - Changes to the Reasonable Endeavours Scheme to better incentivise the detection of Theft, January 2011

¹³ Reducing supplier disincentives to detect and investigate gas theft – Uniform Network Code proposal UNC231V and other changes, Ofgem, 13 December 2010, 104/10

¹⁴ <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?docid=45&refer=Markets/RetMkts/Compl/Theft>

¹⁵ UNC245 - Review of arrangements regarding the detection and investigation of Theft of Gas. <http://www.gasgovernance.co.uk/0245>

Links to other areas

Smart metering

1.24. The roll out of smart meters is expected to have a positive impact on reducing gas theft. Firstly, the replacement of existing metering stock will remove existing meter tamperers and may identify other tamperers to the network that do not involve the meter. Secondly, it is intended that smart meters will be able to provide tamper alerts to give warning that a theft may be occurring. Lastly, more detailed consumption data should enable suppliers to better spot instances where unexpected levels of consumption suggest that there is a risk that a meter is not correctly recording consumption, including where this may be caused by theft¹⁶.

Unaccounted for gas

1.25. Theft of gas is one source of unaccounted for gas. The costs of unaccounted for gas are, to a large extent, paid for by gas shippers and suppliers and therefore passed through to customers. Other modifications to industry arrangements are being made to quantify this level of unaccounted for gas, provide for it to be allocated to the most appropriate parties and to reduce its occurrence. We welcome these efforts and note the following:

- The introduction of arrangements to quantify and allocate an appropriate share of unallocated gas to the LSP market. Previously, the cost of this error (in terms of gas and transportation charges) was borne by SSP shippers only. The reallocation is being facilitated by the appointment of an independent Allocation of Unallocated Gas Expert (the AUGÉ)¹⁷.
- The role of the Shipperless and Unregistered Sites Working Group in developing proposals to reduce the incidence of shipperless and unregistered sites from occurring and arrangements to address them when they do occur¹⁸.

Gas settlements reform

1.26. The gas industry is currently developing proposals to improve its settlement arrangements. These reforms aim to improve accuracy in the allocation of gas and transportation charges. These proposals are being developed in the context of the rollout of smart metering and would allow a customer's charges to better match the consumption of its customers. These changes are currently being discussed under Project Nexus¹⁹. Their focus is on using meter reads (potentially daily meter reads)

¹⁶ New technology may also lead to new mechanisms for theft being developed. It is therefore important that the regulatory framework is capable of responding to this the dynamic nature of gas theft.

¹⁷ Further information can be found at: <http://www.gasgovernance.co.uk/auge>

¹⁸ Further information can be found at: <http://www.gasgovernance.co.uk/industryinfo/UnconSites>

¹⁹ Project Nexus, established by xoserve, aims to work with stakeholders to develop key reforms to current industry processes that support competition in the gas market. It is

to reconcile gas and transportation charges in the SSP market as such arrangements are already in place in the LSP market. In addition, a proposal has been raised to allow the AQ for SSP and LSP sites to update more frequently²⁰. In the context of our proposal to reform the theft arrangements we note that these changes could have a significant impact on a supplier's commercial incentives to proactively detect theft.

Electricity specific proposals

1.27. Electricity suppliers, unlike gas suppliers, have a licence obligation to detect and prevent the illegal abstraction of electricity and damage to equipment²¹. They are required to inspect Non-Half Hourly meters that they supply every two years for evidence of illegal abstraction or damage (SLC12.14). Suppliers also have obligations under the DCUSA to provide information to Distribution Network Operators (DNOs) when they suspect or have evidence of illegal abstraction or damage²².

1.28. In the electricity market, DNOs have strong commercial incentives to reduce the amount of electricity illegally taken²³. DNOs are also required under SLC27 of their licences to provide information to suppliers when they suspect or identify illegal abstraction or damage.

1.29. In October 2009, Electricity North West Limited proposed a change to the DCUSA (DCP054²⁴). This proposal, which is still ongoing, seeks to require each supplier to have in place a Revenue Protection Service²⁵, to have its arrangements audited and for there to be proper governance of the existing Revenue Protection Code of Practice. The aim of this proposal is to ensure that work is undertaken to detect and prevent theft and that found theft is correctly accounted for by settlement arrangements.

1.30. This proposal has been interpreted broadly and has sought to address the lack of incentives that suppliers face in proactively tackling theft. The DCP054 workgroup

expected that that these developments would be proposed through modification proposals to the UNC. For further information see http://www.xoserve.com/nexus_home.asp.

²⁰ UNC380 proposes to update AQs on a monthly basis where new metering data is available, rather than the current annual review process.

²¹ SLC 12.1 "The licensee must take and must ensure that its agents take all reasonable steps to detect and prevent:

(a) the theft or abstraction of electricity at premises supplied by it;

(b) damage to any electrical plant, electric line or Metering Equipment through which such premises are supplied with electricity; and

(c) interference with any Metering Equipment through which such premises are supplied with electricity." See http://epr.ofgem.gov.uk/document_fetch.php?documentid=15664

²² DCUSA clause 30.9 (www.dcusa.co.uk).

²³ As part of the electricity Distribution Price Control 5, DNOs are incentivised to reduce losses (including theft) against a target level. Under this mechanism DNOs would benefit by 6p for every kWh of theft reduction.

²⁴ See <http://www.dcusa.co.uk/Public/CP.aspx?id=68>

²⁵ An organisation with the capability of detecting, investigating and preventing theft.

is for example considering the application of NRPS to electricity. The workgroup has also considered SETS but does not support taking this proposal forward as part of its work. As part of its considerations, the workgroup identified two specific issues that require resolution prior to the introduction of any improved arrangements.

- Theft in conveyance: DCP080 and DCP080A²⁶ have been raised to introduce “theft in conveyance” as a defined term into the DCUSA and to clarify the circumstances where either a supplier or a DNO would have responsibility for charging the customer where theft has occurred from the DNO’s equipment.
- Recording of found units in settlements: A working group under the Balancing and Settlements Code (BSC) has reported to the Panel on a number of proposals to clarify responsibilities to report found units into settlement²⁷. Parties are now considering whether to raise a modification to address this issue.

1.31. The DCP054 workgroup has recognised concerns that the current electricity Revenue Protection Code of Practice is not fit for purpose and has developed a draft code of practice in conjunction with SPAA.

1.32. We will continue to support the development of proposals in the electricity industry. As part of this support we intend to publish a summary, in the next quarter, of key findings from a questionnaire²⁸ that we issued on the existing electricity arrangements²⁹. We are requesting that the industry concludes its deliberations on the options available for reform and brings forward clear proposals by the end of 2011. Once these proposals have been established, we intend to consider the requirement for any changes to licence obligations to deliver improved arrangements. Were we to consult, we would expect to do so by spring 2012.

Structure of this document

1.33. This document is structured as follows:


- In Chapter 2 we set out proposals to introduce new gas supply licence obligations to deliver improvements to the gas theft regime. Our detailed drafting proposals are set out in Appendix 3.
- Chapter 3 summarises three industry proposals to improve theft detection.

²⁶ See <http://www.dcusa.co.uk/Public/CP.aspx?id=98> and <http://www.dcusa.co.uk/Public/CP.aspx?id=110>.

²⁷ See Standing Issue 39 Report <http://www.elexon.co.uk/Pages/Issue39.aspx>.

²⁸ Questionnaire issued by Ofgem to electricity and gas suppliers, DNOs and gas transporters in December 2010. The questionnaire requested information on parties’ experiences in tackling theft over the previous five years.

²⁹ By way of an initial summary, the activity to tackle theft is reported by suppliers to be far higher in the electricity market than in gas. Over the period 2009 and 2010, the average aggregate number of theft investigations conducted by suppliers was approximately 48,000 and the number of theft detections was approximately 19,000 per year. The retail value of the electricity illegally abstracted (attributed to the detected thefts) was approximately £20m per year, of which half was typically recovered.



Tackling gas theft

- Chapter 4 summarises the findings of our draft impact assessment (IA) on the proposals to improve theft detection³⁰.
- Chapter 5 sets out our initial conclusions and the next steps that we intend to take to deliver improved gas theft arrangements.
- Appendix 2 sets out the results of a questionnaire on gas supplier performance that we issued in December 2010.

³⁰ Tackling gas theft: Draft impact assessment, published 31 August 2011. Available on the Ofgem website <http://www.ofgem.gov.uk/Markets/RetMkts/Compl/Theft/Pages/Theft.aspx>.

2. Enhancing obligations on suppliers

Chapter Summary

In this chapter we set out proposals to amend gas suppliers' licence obligations. In doing so, our aim is to establish more effective arrangements for tackling gas theft.

Question 1: Do you agree with our proposals to introduce new gas supply licence obligations in relation to theft?

Question 2: Do you agree that our drafting proposals set out in Appendix 3 meet the policy intent described in this chapter?

Question 3: Do you consider that our proposal for gas suppliers to make reasonable efforts not to disconnect vulnerable customers should apply throughout the year or be restricted to the winter months?

Question 4: Do you consider that gas suppliers should be required to offer vulnerable customers and customers that would have genuine difficulty paying, a wide range of methods for the repayment of charges associated with gas theft as an alternative to disconnection?

Question 5: Do you consider that Ofgem should include a licence requirement on all suppliers to establish a code of practice on, among other things, theft investigations?

Question 6: Do you agree that our proposed new gas supply licence should be introduced as soon as reasonably practical?

2.1. As discussed in the previous chapter, the obligations on suppliers to proactively detect gas theft are, in some cases, weak. While some suppliers consider that they have a commercial incentive to be proactive, this position is not shared by all parties.

2.2. This has led to significant differences between suppliers in their approach to theft detection³¹. While we recognise that there may be differences between supplier portfolios, we consider that there is scope for suppliers to increase their efforts to

³¹ Suppliers have indicated that over the last two years they detected around 2,900 cases of gas theft per year. Information on the number of investigations that were undertaken was less complete but indicates that around 8,100 suspected cases of theft were investigated each year during 2009 and 2010. Supplier data shows that activity between suppliers varies significantly. For example, one supplier was responsible for 70% of the total number of thefts detected and undertook 84% of the total number of investigations over this period. In addition, our analysis indicates that supplier investment over the last two years in tackling theft was £6.5m although the majority was by one supplier. Further detail on the aggregate industry performance data is set out in Appendix 2.

tackle theft to ensure that the industry undertakes a proportionate response to the impact of theft on customers and the market³².

2.3. Our aim is to put in place effective and proportionate arrangements to tackle theft. To facilitate this, we propose to introduce new licence obligations on gas suppliers which set out requirements in relation to the detection, prevention and investigation of gas theft.

2.4. We are requesting views on our proposals, set out in this chapter, to introduce new licence obligations. We are also requesting views on our proposed licence drafting set out in Appendix 3.

The objective

2.5. We propose to introduce an overarching objective to require suppliers to detect, prevent and investigate theft. The obligation would apply to any premises where the licensee is the registered supplier³³. This will require suppliers to cooperate with other licence holders where necessary and ensuring that when a supplier undertakes steps to meet its requirements, its behaviour and actions towards customers are fair, transparent, not misleading, appropriate and professional.

2.6. We have included damage to equipment as well as theft of gas as we consider that damage may also lead to unrecorded gas consumption and potential safety concerns. We consider that suppliers should therefore make efforts to identify damage, remedy it and prevent it from occurring in the first place. For clarity, our proposal in relation to theft of gas described below also relate to damage to equipment unless explicitly stated.

2.7. The aim of the objective is intentionally broader than the offences created under Schedule 2B of the Gas Act. We consider that suppliers should have a general requirement to be vigilant in protecting customers from the impacts of theft and damage to equipment. However, we note that where the gas supplier is not registered to a site, it would meet its requirements if it provided information to the

³² If all suppliers performed to a similar standard as those that have invested in proactive theft detection, we would expect the current performance to lead to the identification of approximately 5,900 thefts per year and for the number of investigations to be in the order of 17,100.

³³ We have linked a supplier's requirements to premises where they are the registered supplier under the relevant gas transporter's Network Code. In light of the implications for deemed contracts, we have deliberately decided not to use the term Relevant Gas Supplier which is a defined term under the gas supply licence and relates to the supplier that is supplying gas to premises. Ofgem's view is that a deemed contract will only arise once a supply of gas is taken, ie when gas has flowed. Therefore, it could be conceivable that, where gas has not flowed, there is no Relevant Gas Supplier for the premises. Our intention is that the supplier registered to that site under the gas transporter's network code would still be required to meet obligations relating to theft in relation to those premises.

gas transporter³⁴. In the remainder of the licence we set out explicit requirements that the supplier would need to undertake to help meet the objective.

Duty to detect and prevent

2.8. We propose to support the new objective with explicit requirements on a supplier to detect and prevent theft of gas at premises where it is the registered supplier.

2.9. We consider that suppliers should make reasonable efforts to detect any damage to equipment or theft at premises where they supply including upstream of the ECV. If a supplier considers that theft or damage has occurred upstream of the ECV, then we consider that it is likely that a supplier will have discharged its obligations if it informs the gas transporter, whose responsibility it is to investigate, in a reasonable manner and within a reasonable timeframe. We would expect suppliers to establish standards for this exchange of information in a code of practice.

2.10. We have modelled this obligation on the arrangements set out in SLC 12.1 of the Electricity Supply Licence. We note that, as with electricity, the obligation is broader than the meter and its immediate installation and relates to theft and damage at premises supplied.

2.11. We consider that “prevent” has two connotations in the context of this licence condition. Firstly, the supplier should stop the theft from continuing to occur once it is identified. Secondly, it should seek to prevent the customer from undertaking theft. This should include measures to deter customers from undertaking this activity and measures to deliver the physical security of the supply. We note that other parties, such as gas transporters will also have responsibilities for aspects of physical security of the network. Our licence proposals are not intended to reduce the requirements of any other party in relation to theft or damage to equipment.

Duty to investigate

2.12. We also propose to introduce a duty on gas suppliers to investigate once they suspect theft of gas. This requirement would not have effect where it was clear that it was the gas transporter’s role to investigate suspected theft in conveyance.

2.13. We consider that this duty would complement obligations to detect and prevent theft. It would seek to ensure that when theft is suspected, reasonable efforts are made to determine whether it had occurred.

³⁴ SLC 17.3 places a requirement on gas suppliers to provide information to the gas transporter on actual or suspected theft of gas.

2.14. Recognising that it can be difficult, in practice, to identify evidence of theft once it is suspected, we propose that this obligation would require a supplier to take all reasonable steps to determine whether an illegal supply has been taken. If introduced, we would expect suppliers to set out standards for the quality of investigations in a code of practice. We are also proposing to establish explicit standards for the treatment of customers within the licence and these are discussed later in this chapter.

Introducing a new arrangement for theft detection

2.15. In Chapter 3 we summarise three industry schemes to improve gas theft detection. Our proposal would allow Ofgem to direct what arrangements should be implemented to increase theft detection. Our intention would be to set out the key elements of the chosen scheme within the Ofgem direction. Our proposals would also set out a timeframe within which the scheme must be delivered.

2.16. We intend to place an obligation on gas suppliers to co-operate in the delivery of one of these new arrangements to increase theft detection.

2.17. In addition to the delivery of revised arrangements to detect theft, we are proposing that suppliers co-operate to identify where improvements to these arrangements could be made and implement these improvements where it is proportionate to do so.

2.18. These proposed new obligations reflect our concerns that increased theft detection, while beneficial to customers and the market as a whole, may not be commercially desirable for an individual supplier. This is potentially illustrated by the lack of progress historically.

2.19. Our initial view is that the requirement on gas suppliers to cooperate to introduce a new arrangement for the detection of theft may not be necessary for one of the proposals (the Supplier Energy Theft Scheme, or "SETS"), given that this is a fully defined proposal under the UNC. In this instance, Ofgem would secure implementation by approving the proposal (this is discussed further in Chapter 3). However, we would welcome views on whether, if the SETS proposal was to be approved, we should retain the elements of our proposal that would require suppliers to consider whether changes to the arrangement should be made, in cooperation with other suppliers where necessary, to meet the requirements of the objective.

Standards of customer treatment

2.20. In this section we propose requirements for gas suppliers on the treatment of customers when investigating a suspected gas theft. In particular, we set out specific proposals for the treatment of vulnerable customers and those that are likely to have genuine difficulty in paying charges. We are proposing minimum standards for the provision of information to customers and the standard of proof required before a supplier takes action to disconnect or levy charges on a customer associated with a theft of gas. We also set out proposals to distinguish the treatment of customers

where a theft has occurred from the debt provisions set out in SLC27 (Payments, Security Deposits and Disconnections). Finally, we consider whether suppliers should be required, through licence obligations, to cooperate to establish and maintain a code of practice setting out standards for the treatment of customers, including details of how suppliers propose to meet their new licence obligations, when investigating a suspected theft.

2.21. For clarity, our proposals also relate to the actions of any agent or representative of the supplier.

2.22. We intend to monitor supplier behaviour on theft investigations. We are working with suppliers to detail specific reporting requirements as part of our discussions on the theft code of practice. In addition, we will be writing to suppliers requesting information on the number of theft disconnections.

Vulnerable customers

2.23. In addition to Ofgem's recent proposals on disconnections in relation to smart meters³⁵, we propose that suppliers should be required to take all reasonable steps to identify vulnerability before considering whether to disconnect a customer on the grounds of theft³⁶. Wherever possible the goal should be to maintain supply to customers identified as vulnerable. Once identified, we are therefore proposing that suppliers take all reasonable steps not to disconnect these customer groups during winter. Our proposals focus on the winter months as the potential consequences for vulnerable customers could be greatest during these months. This proposal is also in line with the debt and disconnection prohibitions set out in the gas supply licence³⁷ which relate to the winter months. Nonetheless, we are requesting views on whether this requirement on suppliers should be extended so that it applies throughout the year.

³⁵ In support of the rollout of smart metering, we are consulting on strengthening consumer protections. Our proposals would include requirements for suppliers to have regard to guidance provided by Ofgem on identifying the status of customers prior to disconnection. We would expect suppliers to take this guidance into account, as appropriate, in the context of our proposals on theft and embed them in the proposed code of practice where relevant. We would also expect to take this guidance into account, as appropriate, when investigating compliance under our proposed licence modifications. See Smart Metering Consumer Protections Package – Statutory Consultation, published 30 June 2011 <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?file=Smart%20Metering%20Consumer%20Protections%20Package%20-%20Statutory%20Consultation.pdf&refer=Sustainability/SocAction/Publications>.

³⁶ ERA suppliers have established a Safety Net commitment - not to knowingly disconnect a vulnerable customer. <http://www.energyretail.org.uk/preventingdisconnection.html>. In addition, Ofgem published its "Review of protection for vulnerable customers from disconnection" in October 2009 (Ref: 121/09). <http://www.ofgem.gov.uk/Sustainability/SocAction/Publications/Documents1/Review%20of%20vulnerable%20customer%20disconnections%20report.pdf>.

³⁷ See SLC27.10 and 27.11 http://epr.ofgem.gov.uk/document_fetch.php?documentid=15667.

2.24. Our proposals would require suppliers to offer to recover any charges associated with the gas theft via a prepayment meter, unless it is not safe or reasonably practicable in all of the circumstances to do so³⁸. We are also requesting views on whether it would be appropriate in the case of gas theft to require suppliers to offer vulnerable customers a wider range of payment arrangements as an alternative to disconnection, in particular, whether it would be practical for suppliers to offer to enter into regular repayment arrangements or for payments to be deducted from social security benefits³⁹.

2.25. Suppliers have powers to disconnect customers and demand charges when, on the balance of probabilities, a theft offence has occurred. This is a decision that a supplier would take rather than a court. The consequences of this action for customers are likely to have a high impact, for example in terms of heating and cooking. Our proposals reflect our view that, for some groups of customers, the consequences can be more severe and potentially life threatening. We consider that this obligation should be supported by a code of practice that established, among other things, clear rules for the treatment of vulnerable customers, to ensure that an increase in theft detection activity does not have an undue impact on these customers. The code should include, for example, procedures for identifying vulnerable customers and fitting prepayment meters instead of disconnection.

2.26. In some circumstances, for example where a vulnerable customer repeatedly tampers with their gas supply and puts themselves or others in danger, then disconnection may be an appropriate response⁴⁰. In so doing, we would expect suppliers to notify the relevant authorities (eg Social Services). This should be done at the time of disconnection, where possible. This would allow the relevant authorities to make alternative arrangements for the vulnerable individual or anyone else in the house being put in danger by the tampering. We consider that suppliers should work together to set out common rules in the code of practice for tackling these situations in conjunction with customer representative bodies.

Customers in payment difficulty

2.27. Prior to disconnection or a demand being made for charges where an offence has occurred, we propose to require that suppliers should seek to identify customers that may have genuine difficulty in paying charges. For the avoidance of doubt, this

³⁸ Our 30 June 2011 consultation on smart metering consumer protections noted above also proposes that suppliers should have regard to guidance provided by Ofgem on the interpretation of when it is safe and reasonably practicable to fit a prepayment meter. We would similarly expect suppliers to take this guidance into account, as appropriate, in the context of our proposals on gas theft and we would consider it in relation to any investigation on licence compliance.

³⁹ See for example gas supply licence SLC27.6(a)(i) and SLC27.6(a)(ii).

⁴⁰ A decision on whether to disconnect on grounds of safety is likely to be made by the gas transporter rather than the supplier. However, a supplier may choose to exercise its powers to disconnect where an offence has occurred and the matter has not been remedied (eg where outstanding charges have not been paid).

would include charges associated with the offence committed such as the cost of the investigation or a meter exchange.

2.28. In instances where such a customer has been identified, we propose to require that suppliers should seek to keep the customer on supply by offering to recover any charges associated with the gas theft through a prepayment meter. As above, in relation to vulnerable customers, we are requesting views on whether suppliers should be required to offer a wider range of repayment methods in addition to prepayment meters, such as entering into regular repayment arrangements or for payments to be deducted from social security benefits. We also consider that suppliers should act in accordance with the recommendations of Ofgem's debt review key principles⁴¹. For example, a supplier should not insist on substantial upfront payments before reconnection where the customer would not be able to make this payment or by doing so would put them in serious financial hardship.

Determination of an offence

2.29. The consequences for a customer if its supplier incorrectly considers that theft has occurred are significant. These include disconnection and requests to repay charges including the cost of the investigation and meter works. Our proposals therefore require suppliers to ensure that they have sufficient evidence to establish that theft has occurred before disconnecting the customer or seeking to recover any charges associated with the offence⁴².

2.30. Our proposals reflect the difficulty that some customers currently face in challenging a supplier's decision. Where there is a dispute over whether an offence has occurred then this may currently need to be resolved through the courts which may be prohibitive for some customers in terms of time, cost and effort required.

Customer communications

2.31. We consider that customers should be provided with timely (ie on the doorstep) and appropriate information during any theft investigation and subsequent follow-up where theft is detected. This would help customers to understand what action is being taken, why and how it can be challenged.

2.32. We are therefore proposing a new licence condition on gas suppliers to ensure that customers are informed who is undertaking the investigation and why, on what basis a supplier considers that an offence has been undertaken, the basis of any

⁴¹ See Appendix 1 of Ofgem's Review of suppliers' approaches to debt management and prevention, published June 2010 - (Ref: 69/10)
<http://www.ofgem.gov.uk/SUSTAINABILITY/SOCACTION/PUBLICATIONS/Documents1/Debt%20Review%20Report.pdf>.

⁴² Ofgem provided additional guidance on the use of disconnection powers relating to theft in October 2010.
[http://www.ofgem.gov.uk/Markets/RetMkts/Compl/Theft/Documents1/Open%20Letter%20on%20Theft%20Disconnections%20\(Final\).pdf](http://www.ofgem.gov.uk/Markets/RetMkts/Compl/Theft/Documents1/Open%20Letter%20on%20Theft%20Disconnections%20(Final).pdf)

assessment of charges made by the supplier, what the customer could do to reinstate their supply following any disconnection and how to challenge the supplier's decision⁴³.

Clarification of disconnection provisions in SLC27

2.33. The current drafting of SLC27 (Payments, Security Deposits and Disconnections) does not provide a robust framework for the protection of all vulnerable customers and customers that have a genuine difficulty in paying charges where a theft has occurred. It is only those customers that have an existing debt that are covered by the prohibition on disconnections (SLC27.9 to 27.11). For example, if a vulnerable customer did not already have a debt with its current supplier then the licence would not prohibit disconnection during winter⁴⁴ on grounds of theft. However, if there was an outstanding debt then a disconnection on grounds of debt would not be permitted.

2.34. We propose to amend SLC27 in recognition of the more targeted customer protections noted above that specifically deal with theft of gas. Our proposal would clarify that the prohibitions on disconnection under SLC27 do not apply where a supplier is using its specific disconnection powers on theft. Our proposals seek to place appropriate safeguards for the protection of specific groups while recognising that an offence has occurred and that there are costs and safety implications for other customers.

Code of practice for investigations

2.35. We consider that suppliers should establish a code of practice on, among other matters, a common approach for the conduct of investigations and the measures that suppliers would undertake to meet the proposed new licence obligations on customer treatment. Such a code should allow suppliers to achieve higher standards where appropriate. All three industry proposals noted in the next chapter support this aim.

2.36. A proposal to introduce a code of practice is currently being developed under the SPAA arrangements⁴⁵. In this context we are not proposing to introduce a licence

⁴³ The ERA Safety Net (www.energy-retail.org.uk/documents/Disconnection_AW2.pdf) sets out the commitments of large suppliers not to knowingly disconnect vulnerable customers on grounds of debt. These guidelines set out standards for follow-up with customers that have been disconnected to understand whether these customers are vulnerable. We consider that these standards should be adopted in relation to customers that have been disconnected on grounds of theft. We would welcome the inclusion of these requirements and consideration of the follow-up requirements in the proposed code of practice for theft investigations.

⁴⁴ We note and welcome the commitments provided under the ERA's Safety Net not to disconnect vulnerable customer at any time of year, where for reasons of age, health, disability or severe financial insecurity, that customer is unable to safeguard their personal welfare or the personal welfare of other members of the household.

⁴⁵ Certain protected provisions within the SPAA cannot be changed without Ofgem's consent. Given the potential impact of the proposed code of practice on customers we would expect

condition on suppliers to establish a code at this stage. However, we would give further thought to this if such a code was not to be forthcoming.

2.37. We consider that the code of practice should apply to both the domestic and non-domestic markets⁴⁶. We note that compliance with SPAA is not a licence requirement for non-domestic suppliers. We intend to separately propose an amendment to the standard conditions of the gas supply licence to make compliance with the relevant sections of SPAA an obligation for all licensed suppliers.

2.38. In the context of these developments we would welcome views on the need for a licence obligation to establish a code of practice.

2.39. To facilitate the continued alignment of the proposed code of practice with the objectives of the SPAA, where that document is proposed to sit, we propose to amend the relevant objectives of the SPAA. This change would insert a new relevant objective to secure compliance with the requirements of the new supply licence obligations on gas theft. We consider that this would provide a point of reference for any related changes to the SPAA and would also require parties to make efforts to ensure that the SPAA facilitated the requirements of the new theft licence condition⁴⁷. We also consider that such a change would also be of benefit were the NRPS or elements of the Enhanced SETS proposals, described in the next chapter, to be inserted into SPAA.

Implementation and links to reform in the electricity market

2.40. As the issues are likely to be similar across both gas and electricity, some parties may consider that we should also be proposing changes to the electricity market to align any enhancements to customer protections. Our intention is to align the consumer protections on gas and electricity where necessary. However, we intend to review this once the broader proposals for reform in the electricity market are clearer. We consider that there are benefits in proposing the changes now to the gas market as the specific proposals to increase theft detection are more developed.

that Ofgem would be responsible for approving the code and any further modifications to it. We would also expect the industry to consult broadly on its proposals (and any subsequent modifications) including with consumer representative groups and we would expect to take this into account when making a decision.

⁴⁶ We further consider that equivalent arrangements should be extended to gas transporters, and to electricity suppliers and distributors.

⁴⁷ SLC 30.5 of the gas supply licence requires a supplier to take all reasonable steps to ensure that the SPAA remains an agreement which facilitates its relevant objectives. (See http://epr.ofgem.gov.uk/document_fetch.php?documentid=15667).

Compliance and management arrangements

2.41. We propose that suppliers and their representatives must retain information on how they (and their representatives) have complied with their obligations under the new licence condition.

2.42. We also propose that suppliers must put in place management arrangements to ensure that their agents or any other subcontractors meet the requirements of the new licence condition.

3. Industry proposals to improve detection

Chapter Summary

In this chapter we describe the key features of three schemes proposed by the industry to increase theft detection.

3.1. In response to our call for action, industry participants have put forward three distinct proposals that aim to improve gas theft detection. These proposals are described below.

3.2. We are requesting views in Chapter 4 of this consultation on which, if any, of these proposals should be implemented. To assist this discussion we have produced a draft IA which is published alongside this document. The findings of this initial assessment are summarised in the next chapter.

National Revenue Protection Scheme (NRPS)

3.3. The NRPS proposal, developed by a Gas Forum⁴⁸ workgroup, was presented to Ofgem on 16 June 2011. Its premise is that theft can be more efficiently detected if it is tackled collectively by the industry. The proposal considers that there are efficiency gains in analysing data centrally within the industry rather than each supplier operating separately.

3.4. The main feature of the NRPS proposal is the operation of a single, central database to profile all gas customers and identify, using risk-based analysis, sites that should be investigated. This investigation is intended to be a physical visit to the premises to understand whether theft is occurring/has occurred, or any other problem has caused the meter to not fully record the amount of gas consumed.

3.5. The aim of this single, central database is to pool industry data and other relevant data sources together with analytical resources to target those sites with the highest risk of unrecorded consumption, in particular related to theft of gas. Suppliers would then be required to investigate when asked to do so by the NRPS.

3.6. In response to concerns about access to services to tackle theft (eg field investigation and debt recovery), in particular for smaller suppliers, the NRPS would also be required to ensure that such services are available to suppliers. This is intended to be a separate activity from the data analyst function.

⁴⁸ The Gas Forum is a body that represents the views of many of the gas shippers and suppliers active in the GB Market. www.gasforum.co.uk

3.7. While the NRPS proposal is non-specific on the absolute performance expected in detecting theft, the Gas Forum report refers to the potential performance that could be achieved if all suppliers performed to the standards of the highest performing suppliers currently in the market. Based on this expectation we have assumed that the NRPS would be expected to provide 17,000 leads for suppliers to investigate per year and for this to deliver approximately 6,000 cases of identified theft.

3.8. After an initial period of two years it is intended that the NRPS would be incentivised to improve the quality of leads for investigation that it provides to suppliers. In particular, it would be expected to improve the conversion rate between investigations and thefts detected (or potentially other causes of unrecorded gas). However, no explicit target has been established at this stage.

3.9. An audit function is proposed to ensure that the theft leads provided by the NRPS are investigated by suppliers' agents to the agreed standards (set out in a code of practice) and that customers are treated in an appropriate and consistent manner.

3.10. Detailed information on the scope of the NRPS proposal is set out in a document provided by the Gas Forum workgroup⁴⁹. The workgroup recognised the concerns that some parties may have in relation to data protection and commissioned legal advice on this issue. This legal advice concluded that data protection and privacy is an important issue and that a Privacy Impact Assessment should be conducted by suppliers to demonstrate whether the data held was proportionate. Nevertheless the advice was that the concept of a central database to identify the risk of gas theft was still valid. The Gas Forum has committed to conduct an independent Privacy Impact Assessment to Ofgem within sufficient time to inform our decision.

Summary of key features

3.11. The key features of the NRPS proposal are as follows:

- **Data source:** Suppliers and gas transporters would be required to provide data to a central body (the NRPS). Data would also be sought from other available sources.
- **Data analysis:** The NRPS would analyse data to provide a risk profile for each meter point. This profiling would identify sites which, based on industry-agreed criteria, should be investigated to ensure that consumption is being correctly recorded, and in particular whether a theft has taken place.
- **Investigations:** All suppliers would be required to investigate the cases nominated by the NRPS and to do so in accordance with a code of practice.
- **Customer treatment:** Standards would be established under a code of practice. These would include estimating unrecorded consumption, debt recovery and case preparation for prosecution.

⁴⁹ NRPS Workgroup Report to Ofgem, 16 June 2011. Gas Forum
www.gasforum.co.uk/admin/documents/GF%20NRPS%20Final%20Report%20v1.0.pdf

- **Service provision:** The NRPS would be required to provide investigation, debt recovery and prosecution services to suppliers on request. However, suppliers may source these services internally or from third party providers. Charges for these services will be made on the basis of costs plus an agreed margin.
- **Industry revenue accounting:** Industry rules for the allocation of energy and transportation charges would be amended to correct the AQ once theft has been identified. This seeks to improve the allocation of energy and transportation charges prospectively but would not impact on any previous misallocation.
- **Performance assurance:** To provide for a consistent approach for customers and industry parties. Audit provisions would monitor compliance by suppliers and the NRPS (when it provides services on a supplier's behalf). An audit would also be performed on the NRPS to, amongst other things, ensure compliance with data protection provisions.
- **Other supporting measures:** The NRPS would establish a 24-hour hotline for tip-offs on suspected gas theft to be reported by members of the public as well as a register of stolen meters.

Incentives

3.12. Over the initial period it is expected that the performance of the NRPS as provider of data services would be measured against a number of key performance indicators, including the conversion rate between investigations and detected theft. It is expected that the reward structure would be revisited after two years once a base case performance level has been derived and incentives would be introduced to improve performance.

3.13. As noted above, each supplier would be subject to audits on their performance in meeting set standards, for example on the quality of investigations. The aim of the audit framework is to incentivise supplier performance in meeting the required standards. If a supplier was not able to demonstrate compliance, it would be required to pay the audit costs and make any relevant rectifications to ensure compliance.

Governance

3.14. Under this proposal, suppliers would be required, by obligations set out in their supply licences, to comply with an industry code that established and maintained the NRPS.

3.15. Two broad options have been proposed for how these industry arrangements could be achieved. One is to introduce a new mandatory schedule into SPAA. The alternative is to introduce a new industry code⁵⁰. For the purpose of our analysis we have assumed that the arrangements would be introduced into SPAA, with all suppliers (including non-domestic suppliers) required to comply with the relevant

⁵⁰ The UNC, which is an agreement between shippers and large gas transporters, was considered not to be a suitable vehicle given the focus of the proposed NRPS arrangements on the relationship between suppliers and gas customers.

sections of SPAA. Our view is that the time and resource required to establish new governance arrangements could be significant and that adding a new governance framework to the industry arrangements is likely to increase complexity in the market.

3.16. Introducing the NRPS into SPAA would require a change to the licence obligations to require non-domestic suppliers to be a party to this agreement and comply with the relevant sections. Amendments would also be required to the SPAA governance arrangements to facilitate non-domestic supplier members, and we will shortly set out our proposals to amend the gas supply licences to facilitate this change.

3.17. We note that amending the SPAA arrangements is a potentially lengthy process. We would welcome work by industry parties to develop the detailed changes required to amend the SPAA governance arrangements in parallel with this consultation.

Costs and implementation

3.18. The cost of implementing the NRPS data analysis function would be the subject of a competitive tendering exercise. However, our analysis, which is set out in our draft IA, suggests that the costs of this and the subsequent investigations would range between £6.8m and £10.1m per year and would have set up costs of between £1.5m and £3m.

3.19. The Gas Forum group has estimated that it would take around 12 months from a decision to proceed until the NRPS was ready to go live. The group indicated that this timescale would be dependent on work being initiated during this consultation phase. For the NRPS to be delivered, the industry would need to tender for and appoint the NRPS service provider⁵¹. The NRPS service provider would need to ensure that it had in place measures to fulfil its functions, including the offer of field investigation forces on request. Detailed operational arrangements would need to be developed for the NRPS and suppliers. The SPAA governance arrangements would need to be amended to incorporate non-domestic suppliers and associated arrangements would need to be inserted within the scope of the SPAA.

Supplier Energy Theft Scheme (SETS)

3.20. SETS has been proposed by British Gas and developed as two modifications to the UNC. SETS places a financial incentive on a supplier (through its shipper) to detect and report gas theft, including damage to equipment.

⁵¹ There is some uncertainty here on whether this tendering exercise should be taken forward under SPAA once non-domestic suppliers had become parties to the agreement. We note that this would delay the initiation of this process. An alternative view is that the tendering process could be initiated separately, for example through an off-the-shelf company, which could novate to SPAA in due course.

3.21. Under the proposal a shipper would be required to fund the incentive scheme in accordance with its market share. It would then be eligible for incentive payments in line with its relative performance in detecting theft

3.22. Two alternative mechanisms have been proposed to determine a shipper's market share. This market share measure is the substantive difference between British Gas's two different UNC modification proposals: UNC277 and UNC346.

- **UNC277:** market shares are based on the number of Supply Points⁵² in a shipper's portfolio at the end of each scheme year. The level of identified theft attributed to the shipper would be calculated using the number of thefts reported.
- **UNC346:** market shares are calculated on the basis of throughput for the shipper portfolio. The level of identified theft for each shipper would be based on the volume of stolen units reported.

3.23. Note that this proposal does not include Daily Metered sites⁵³ as such sites were already considered to be subject to sufficient scrutiny. Very small shippers⁵⁴ are also excluded.

3.24. British Gas has indicated that SETS would deliver at least 5,913 confirmed gas thefts and that this would result from at least 17,100 theft investigations per year⁵⁵.

3.25. Further detail on UNC277 and UNC346 can be found in the Final Modification Reports (FMRs) published by the Joint Office⁵⁶ on 21 January 2011⁵⁷.

Summary of key features

- **Data source:** Shippers would not be required to share data but would be incentivised to access all relevant, available data sources.
- **Data analysis:** Each shipper would be responsible for securing its own data analysis (either internally or through a third party) and would be incentivised to innovate.
- **Investigations and customer treatment:** This proposal does not explicitly determine the manner in which an investigation should take place. However, the proposal references that investigations are expected to take place in accordance

⁵² A Supply Point is defined under Section G1.1.1(a) of the UNC. It describes a meter point (or aggregation of meter points that meet set criteria) registered to a shipper

⁵³ Sites with an annual consumption of greater than 58.6GWh.

⁵⁴ Under UNC277 and UNC346 a supplier whose market share when expressed to four decimal places is zero would be excluded from the scheme. Under UNC277 this approximates to shipper with around 110 supply points and under UNC346 it equates to a shipper with a yearly throughput of 2.6GWh.

⁵⁵ This figure is higher than that originally set out by British Gas in its consultation response on UNC277 and UNC346. British Gas has revised its estimate based on improved data on current performance standards following Ofgem's questionnaire at the end of 2010.

⁵⁶ The Joint Office administers the governance arrangements for the UNC.

www.gasgovernance.co.uk/About

⁵⁷ See www.gasgovernance.co.uk/0277 and www.gasgovernance.co.uk/0346.

with a code of practice⁵⁸ and claims for incentive payments would be audited against this code. A failure to adhere to the industry standards in the related code of practice would impact on incentive payments. This code is currently in development under the SPAA governance arrangements.

- **Service provision:** Shippers would be expected to secure service provision internally or through third party service providers.
- **Customer treatment:** This proposal does not explicitly determine the manner in which an investigation should take place although, as noted above, additional measures are expected to be established under a SPAA gas code of practice and shippers would be penalised where the audit revealed non-compliance with the proposed code of practice.
- **Industry revenue accounting:** The current settlement rules would not be amended under this proposal.
- **Performance assurance:** An auditor would be appointed to sample shippers' claims of identified theft against the Gas Act as a standard of proof (ie whether on the balance of probabilities the customer committed the offence) and the code of practice. Where such claims cannot be substantiated, or where non-compliance with the proposed code of practice was identified, the shipper would be penalised. It is proposed that the total number/volume of reported thefts would be reduced in proportion with the level of unsubstantiated cases identified by the auditor in its sample. This would then impact on the credit/debit that the shipper would achieve under the scheme.

Incentives

3.26. The aim of SETS is to encourage suppliers to be proactive in detecting theft. The scheme would reward suppliers (via their shippers) when they identify theft. SETS encourages suppliers to invest in theft detection or transfer funds to those suppliers that do so.

3.27. The proposer acknowledges that those suppliers that have already invested in proactive theft detection may have an advantage over the initial period of the SETS arrangement. To mitigate this issue, a "Windfall Avoidance" measure has been proposed over the first two years of SETS. Over this initial two year period, British Gas would be excluded from receiving credits and debits but would still be subject to the audit and reporting measures. The value of the incentive scheme will be reduced to account for this exclusion over the first two years of the scheme.

Governance

3.28. The SETS proposal has been raised as a change under the UNC. It would therefore become part of the industry code between the large gas transporters and shippers operating on their networks.

⁵⁸ The proposer intends that SETS is supported by a code of practice under the SPAA arrangements, although this is not essential to the proposal. As set out above, we note that non-domestic suppliers are not required to sign and comply with SPAA under the terms of their licences. However, we are proposing an associated change to the SPAA governance arrangements to address this issue.

3.29. SLC3 of the gas shippers licence places requirements on gas shippers in relation to their use of a gas transporter pipeline under the UNC. In addition, the SETS audit function, with its proposed financial sanctions, has been developed to take action when a shipper's claim to have detected theft cannot be substantiated to the auditor and it has not met the requirements of the proposed code of practice.

Costs and implementation

3.30. The value of the scheme has been calculated by extrapolating the proposer's costs in tackling theft. For UNC277 this provides a total annual pot of approximately £10m per year. Under UNC346 the value of the scheme is around £12m per year. The value of both proposals would be linked to inflation.

3.31. It is intended that the transporters' agent (xoserve) would be the System Administrator. The System Administrator would appoint an auditor to ensure the validity of shippers' claims and its compliance with the proposed code of practice. A mechanism for reducing a shipper's incentive payment is proposed when the Auditor finds instances where a shipper is not able to provide sufficient evidence that it has complied with its requirements.

3.32. Analysis presented in the FMR for UNC346 estimates that SETS would have set up costs of £200-380k and ongoing annual operational costs of £40-80k. It is expected that the audit costs would be approximately £50k per year. These would be additional to the operating costs of the System Administrator.


3.33. Xoserve has estimated that delivery of the System Administrator role would take between 35 and 51 weeks. This development could take place in parallel with operation of SETs during its first year. These timescales do not include the tender process for the appointment of the Auditor (which could also be conducted in parallel).

3.34. For either UNC277 or UNC346 to have effect, Ofgem would need to approve the relevant modification to the UNC. In doing so, we would assess the modification proposals against the relevant objectives of the UNC and consider whether they were consistent with our statutory duties.

Enhanced SETS

3.35. Enhanced SETS has been proposed by British Gas⁵⁹. It builds on the SETS incentive mechanism described above. In addition to SETS and a code of practice for theft investigations, it proposes two options for adding additional services to help suppliers detect theft:

⁵⁹ The Creation of a Revenue Protection Activity Co-ordination Agent (RPACA) and a Central Revenue Protection Unit (CRPU), 8 April 2011. British Gas. See www.ofgem.gov.uk



Tackling gas theft

- Option A: A Revenue Protection Activity Co-ordination Agent (RPACA)
- Option B: In addition to the RPACA, a Central Revenue Protection Unit (CRPU)

3.36. The role of the RPACA is to provide services that would benefit from coordination between industry parties. In particular, these include:

- Management information on the location of theft and how it occurs
- Provision and management of a National Theft Hotline
- Management of a stolen meters register
- Coordination of the handover of investigations between suppliers during the change of supplier process
- Facilitation of discussion between the industry and non-industry parties with an interest in gas theft
- Sharing of best practice throughout the industry

3.37. The role of the CRPU would be to enter the market to offer services to suppliers to help them respond to the incentive scheme set up under SETS. The services offered by the CRPU would include:

- Collection and processing of data for the purposes of lead generation and risk profiling
- Field services for physically detecting and resolving theft
- Provision of debt and revenue recovery services
- Provision of legal services
- Provision of settlement management services
- Ongoing management of sites where theft has occurred

3.38. Suppliers would be able to use the CRPU or separately contract for these services.

Summary of key features

3.39. For the purpose of this section we have noted the differences and additional functionality of Enhanced SETS compared with SETS and the proposed code of practice.

- **Data source:** Suppliers would be required to share management data on the location and type of thefts identified. Suppliers may also be required to provide information on theft where a change of supply has occurred.
- **Data analysis:** The RPACA would provide management information for use by suppliers. Under Option B, suppliers could additionally contract with the CRPU for the provision of data analysis services.
- **Investigations and customer treatment:** Under Option B a supplier could contract with the CRPU for the provision of field investigation services.
- **Service provision:** Under Option A, suppliers would be expected to secure service provision internally or through third party service providers. However, under Option B, suppliers could seek to secure additional services to support their theft detection work through the CRPU.

Incentives

3.40. The Enhanced SETS proposals are not expected to alter the overall incentive framework provided by SETS. The RPACA proposal aims to reduce the negative impact of any incentive on a supplier under SETS not to share management information or best practice with the aim of gaining a competitive advantage.

Governance

3.41. British Gas considers that a requirement on suppliers to establish the RPACA and CRPU, to set out the required standards and comply with requirements, where necessary, should sit in the SPAA.

3.42. British Gas considers that the articles of association allow SPAA Ltd to become the contracting vehicle for these services and for it to manage the contract on an enduring basis.

Costs and implementation

3.43. British Gas estimates that the cost of providing the RPACA functions would be low, in particular, if this service is provided by xoserve. British Gas argues that xoserve would be able to offer synergies with the current information services offered to suppliers, in particular, it has experience in running customer telephone lines for the reporting of information (such as the current 0800 111 999 service) and is able to provide data on change of supply. British Gas also considers that the cost of maintaining a stolen meters register, co-ordinating industries efforts with external agencies or providing a forum for best practice discussions would not be high.

3.44. It notes that the services under the CRPU are likely to be more substantial but consider that they would be offered on a competitive basis such that the total value of suppliers' investment in theft detection is not likely to exceed the £10m value of the UNC277 incentive scheme. This view is based on an assumption that investment in theft detection will match the returns available. We have assessed this assumption further in the accompanying IA.

3.45. In terms of implementation, British Gas expresses a preference for the RPACA to be delivered by xoserve and consider that this could be delivered within nine months. It notes that the RPACA service provider could also be appointed through competitive tender and it is likely to require a longer implementation period. British Gas estimates that the CRPU service could be live within approximately 18 to 24 months of an Ofgem decision. British Gas envisages that SETS, RPACA and CRPU could be introduced in phases as they became ready rather than necessarily all having to be implemented at the same time.

4. Assessment of industry proposals

Chapter Summary

This chapter summarises the key findings of our draft impact assessment of three industry proposals to increase theft detection. We have given particular attention to potential differences identified in the impacts of each of these proposals and highlighted the main areas where we are seeking further information.

Question 7: Have we correctly assessed the main impacts in the accompanying IA? Are there additional, material impacts that we should consider?

Question 8: Do you agree with the assumptions that we have made and the outcome of our analysis in the accompanying IA?

Question 9: Which, if any, of the three proposals to increase theft detection should be implemented and why?

Question 10: Do you consider that there are any alternative proposals, or variations on existing proposals to improve theft detection that should be considered?

4.1. A draft IA on the three proposals to increase theft detection set out in Chapter 3 has been published alongside this consultation. We identify the relative strengths and weaknesses, but we do not present a preferred option. We will use responses to this consultation to help refine our analysis and determine which, if any, of these proposals should be implemented.

4.2. We invite views on whether we have correctly assessed the impacts of the three proposals in the draft IA and whether there are any additional material impacts that we should consider. Further evidence relating to our detailed assumptions and the outcome of our analysis in the accompanying draft IA would be welcome.

4.3. Furthermore, we seek your views on which, if any, of the proposals should be implemented and why. Any responses supporting SETS or Enhanced SETS should be clear as to which variation of the proposals should be implemented⁶⁰. We also welcome suggestions for developing or improving any of the proposals under consideration.

⁶⁰ The possible permutations for SETS would be either UNC277 or UNC346. For Enhanced SETS there would be a choice between UNC277 and UNC346 and there would be an additional choice between implementing the RPACA by itself or implementing both the RPACA and CRPU.

Impacts on consumers

4.4. Our assessment considers the quantitative benefits that customers could achieve through lower bills under each of the three proposals. We also make a qualitative assessment of the proposals, relating to the likelihood that a customer would be investigated, the quality of that investigation and the prospect of an investigation leading to theft detection.

4.5. Some gas charges cannot be recovered from customers who have taken an illegal supply. Consequently, supplier revenues are lowered, while charges increase for other customers as suppliers seek to recover their costs. Any reduction in gas theft is therefore likely to place downward pressure on customer bills.

4.6. Based on an assumed increase in theft detection from 2,900 to 6,000 cases and an estimate of the costs of each proposal, our analysis indicates that costs of operating the NRPS proposal for a single year would achieve break even 17 months after the beginning of that year. SETS and Enhanced SETS would do so after 24 months. If customers continued to pay charges past the break-even point then this would deliver additional benefits of £341,000 per month. These benefits could reduce future customer bills.

4.7. Our assessment focuses on the costs of each proposal. The lower the cost, the shorter the period of attributable future revenue recovery required to break even, and the greater the potential benefits for customers. The potential for each proposal to perform better than our assumed 6,000 thefts from 17,000 investigations is assessed in Chapter 3 of the IA. Our analysis suggests that each proposal would offer an improvement over the current situation, as long as they deliver the assumed number of detections. This conclusion is robust when considered against a number of variations in our assumptions, presented in our IA.

4.8. Given the potential strong positive net benefits for customers from proactive theft detection, we have requested views in the IA on the ability of each proposal to achieve the notional target of 6,000 thefts and whether this target is sufficiently ambitious in the context of the customer benefits that could be delivered.

4.9. Our qualitative analysis indicates that under the NRPS proposal, there may be an incentive to under-record theft if the costs of finding theft outweigh the costs of investigating but not finding theft. SETS and Enhanced SETS have considerable commercial drivers and these may lead to overzealous investigations and potential misreporting of theft. All three proposals would introduce a code of practice to set out standards for theft investigation and would establish audit and penalty provisions. We have requested views in the IA on whether these mitigate any potential concerns.

Impacts on competition

4.10. In addition to the broader costs and benefits under each proposal, we consider the allocation of gas and transportation costs between suppliers. We consider the

effect of including a compensation scheme alongside the three proposals and we then specifically address the competition impacts on smaller suppliers and potential new entrants.

4.11. Using a series of assumptions, our analysis of the allocation of gas and transportation costs indicates that under current arrangements:

- An SSP shipper will benefit from detecting a theft (when compared to not detecting a theft). This benefit is not impacted by the SSP shipper's market share
- Large SSP shippers will benefit more from theft detection by other parties because of their larger contribution to smeared industry costs (although these benefits will be spread across a greater cost base)
- LSP shippers are likely to have a commercial disincentive to detect theft

4.12. The additional incentive payments available under SETS and Enhanced SETS would provide significant commercial incentives for suppliers to detect theft in both the SSP and LSP markets. However, we have concerns that the value of the incentive pot is arbitrary. Rather, it should be considered in the context of the likely number of investigations that would result and the scale of potential benefits for customers. We are also concerned that there are factors that are outside of a supplier's control that would unfairly prejudice their ability to compete on a level playing field with other suppliers. For example, economies of scale in detection and prevalence of theft within the supplier's portfolio could differ significantly between suppliers. We have requested views in the IA on whether these are material factors. In relation to the Enhanced SETS proposal we have requested views in the IA on the extent to which the additional services provided would mitigate any material concerns about a supplier's ability to compete for incentive payments.

4.13. Under the NRPS, suppliers would be required to investigate theft when requested by the NRPS agent. Theft detection often takes considerable skill and diligence on the part of the investigator. The quality of the investigation and follow-up will impact on the costs directly borne by the supplier. In the IA we ask whether the NRPS contains sufficient measures to deliver high-quality investigations in a consistent manner across all suppliers. We also request evidence of how the NRPS is likely to establish targets for overall performance given that the potential benefits are likely to differ between parties and that these may not correlate to the potential benefits of tackling theft for customers.

4.14. At the aggregate industry level, increased theft detection is likely to improve accuracy in the allocation of gas and transportation charges to suppliers. This is expected to have a positive impact, in particular on smaller suppliers and new entrants, in terms of their ability to understand and manage their costs. Smaller suppliers and new entrants could be at a disadvantage in competing for incentive payments under SETS. These effects may be mitigated to some extent by Enhanced SETS. We consider that the NRPS is likely to offer the greatest benefits for smaller suppliers and new entrants in enabling them to tackle gas theft.

4.15. We have considered the potential for suppliers to over-report theft under SETS and Enhanced SETS. We have requested views on whether the audit and

penalty measures for the NRPS, SETS and Enhanced SETS would mitigate the identified risks.

Impacts on sustainable development

4.16. Our assessment suggests that there would be a moderate but positive impact on energy efficiency and reduced carbon emissions associated with increased theft detection. This would be driven by customers that have previously taken an illegal supply facing the full cost of their gas charges once the theft has been discovered and reducing their overall consumption. In the IA we are requesting views on the extent of this effect.

4.17. We also consider that increased theft detection would assist the goal of eradicating fuel poverty and protecting vulnerable customers by reducing bills and improving safety.

4.18. The extent to which each of the effects noted above is realised would depend on the success of the proposals to increase theft detection. As noted above, we are requesting views in the IA on the ability of each proposal to deliver increased theft detection.

4.19. Our initial view is that, over and above the number of thefts detected, there is a limited differential between the proposals in their impact on sustainable development. We consider that, under the SETS proposal, there may be advantages in reduced carbon from focusing on the volume of gas stolen rather than the number of theft incidents.

Impacts on health and safety

4.20. Theft can have a material impact on safety for customers and others in close proximity to the theft. Reducing theft is also likely to improve the security of the gas supply by reducing the likelihood of explosions, damage to the network and other related causes of interruptions. Our view is therefore that an increase in theft detection is likely to improve safety, although we have not been able to quantify this benefit.

4.21. As noted above, we request views in the IA on the ability of each proposal to deliver increased theft detection. We expect to use this information to help us determine whether there is a difference between the ability of each of the three proposals to improve safety.

Risks and unintended consequences

4.22. We have considered whether any of the proposals may give rise to significant risks or unintended consequences that have not otherwise been identified. Our initial view is that these are limited. We seek feedback as to whether we have omitted any risks or consequences.

4.23. We have noted that increased theft activity may increase complaints from customers about their treatment. This is an important area to monitor to ensure that suppliers are operating in accordance with the licence and the proposed code of practice.

4.24. We have identified one further issue that may arise from increased customer awareness of the potential for theft. Increased publicity may bring the concept of energy theft to the attention of parties, in both the gas and electricity markets, that may not have otherwise considered this activity. In particular, both the NRPS and Enhanced SETS proposals would seek to publicise a 24-hour telephone tip-off service. Our initial view is that we would support the publication of an appropriate message to customers that warned them of the dangers of theft and sought to deter them from this activity. However, we consider that this may have consequences for the electricity industry if similar steps are not in place in this market.

Other impacts

4.25. In the IA we considered whether there were any other impacts to those described above that we should consider in making our decision. In particular, we have considered whether there are any elements that help to distinguish the impacts of each proposal.

4.26. Implementation timescales could be one such distinguishing feature. We think the chosen approach to theft detection should be enduring and, so long as the range of proposed implementation dates is reasonably small, we would not expect this to drive material differences in our consideration of the proposals. The SETS proposal is likely to be capable of being implemented within the shortest timescale. The proposers of NRPS expect this solution to be deliverable within a shorter timeframe than the CRPU element of Enhanced SETS. The NRPS would take longer to deliver than the RPACA. Our draft IA requests input on the accuracy and feasibility of these estimated implementation timescales.

4.27. We note that NRPS and Enhanced SETS offer additional features to SETS that would help to increase theft detection and deter theft. In particular, both NRPS and Enhanced SETS would provide a register of stolen meters and the NRPS makes reference to helping to resolve unregistered sites⁶¹.

We consider that all of the proposals are likely to increase the detection of sources of unaccounted for gas in the market. This could include unregistered sites and theft upstream of the ECV, which is the responsibility of gas transporters to investigate. Our IA requests evidence on any impediments that may impact gas transporters' ability to respond.

⁶¹ These are instances where a gas supply is being taken but there is not a registered gas shipper and supplier associated with that site. These are instances where industry processes have failed to correctly register the site rather than theft being associated with physical damage to the network.

5. Conclusions and next steps

5.1. We consider that it is important to establish effective and proportionate arrangements for tackling theft. These need to be both enduring and sufficiently flexible to adapt to changes in consumer behaviour and market developments (such as new settlement arrangements and the rollout of smart meters). We recognise and welcome the significant efforts that industry parties have made to develop innovative solutions to meet these aims. It is important to maintain this momentum and we are committed to facilitating improvements in the market as soon as reasonably possible.


5.2. To assist us in making the necessary improvements to the regulatory framework we are requesting responses by 26 October 2011 on the proposals set out in this consultation for new supplier licence obligations to tackle gas theft and on the three industry proposals specifically aimed at increasing theft detection rates. Further detail on how to respond is set out in Appendix 1.

5.3. Following consideration of responses we aim to set out our decision by the end of 2011. This will include an updated IA. We are requesting comments in Chapter 2 on the timing of the implementation of any modification to the gas supply licence but our initial view is that these should be in place by early 2012.

5.4. In our decision document, we also intend to set out our decision on UNC231V, which proposes changes to supplier compensation arrangements when theft is identified but charges are not recovered from the customer. We will also report on progress to introduce a code of practice under SPAA to address matters including theft investigations by suppliers.

5.5. As noted in previous chapters, Ofgem will shortly be proposing changes to the gas supply licence to require non-domestic suppliers to become parties to and comply with the SPAA. In the context of the theft discussions we consider that this change will help to facilitate the application of the proposed code of practice on theft investigations to non-domestic as well as domestic customers. It would also provide a governance framework for the development of the NRPS or Enhanced SETS, were either of these to be chosen. We intend to set out our decision on this licence modification proposal by the end of 2011 to facilitate implementation in early 2012.

5.6. We expect that the measures proposed in this document will increase the amount of suspected theft identified upstream of the ECV. Gas transporters have licence obligations to investigate such incidents and will need to ensure that they have sufficient resource and appropriate processes and procedures to respond to these requirements. In particular we would welcome the expansion of the proposed gas theft code of practice to cover the actions of gas transporters when conducting theft investigations.



Tackling gas theft

5.7. As noted in Chapter 1, we are continuing to work with the electricity industry to develop proposals for reform. The development of proposals to increase theft detection has slowed while important issues of responsibility are being tackled. We expect electricity suppliers and DNOs to continue to develop robust proposals and we would welcome notification by the end of this year of which proposals are to be actively progressed. We intend to propose changes to align the gas and electricity arrangements where necessary and we will give consideration at this point on what measures Ofgem should undertake to deliver proportionate and enduring arrangements for tackling electricity theft. We expect to consult on proposals in the electricity market by spring 2012.

Appendices

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Appendix 1: Consultation response and questions

1.1. Ofgem would like to hear the views of interested parties in relation to any of the issues set out in this document and in the accompanying IA. We would especially welcome responses to the specific questions which we have set out at the beginning of each chapter heading and which are replicated below.

1.2. Responses should be received by 26 October 2011 and should be sent to:

Margaret Coaster
Smarter Markets
9 Millbank
London
SW1P 3GE
020 7901 7042
margaret.coaster@ofgem.gov.uk

1.3. Unless marked confidential, all responses will be published by placing them in Ofgem's library and on its website www.ofgem.gov.uk. Respondents may request that their response is kept confidential. Ofgem shall respect this request, subject to any obligations to disclose information, for example, under the Freedom of Information Act 2000 or the Environmental Information Regulations 2004.

1.4. Respondents who wish to have their responses remain confidential should clearly mark the document/s to that effect and include the reasons for confidentiality. It would be helpful if responses could be submitted both electronically and in writing. Respondents are asked to put any confidential material in the appendices to their responses.

1.5. Having considered the responses to this consultation, Ofgem intends to set out its decision on whether to propose new licence obligations for gas suppliers and on which, if any, of the three proposals to increase theft detection should be implemented. Any questions on this document should, in the first instance, be directed to:

Andrew Wallace
Smarter Markets
9 Millbank
London
SW1P 3GE
0207 901 7067
andrew.wallace@ofgem.gov.uk

CHAPTER: Two

Question 1: Do you agree with our proposals to introduce new gas supply licence obligations in relation to theft?

Question 2: Do you agree that our drafting proposals set out in Appendix 3 meet the policy intent described in this chapter?

Question 3: Do you consider that our proposal for gas suppliers to make reasonable efforts not to disconnect vulnerable customers should apply throughout the year or be restricted to the winter months?

Question 4: Do you consider that gas suppliers should be required to offer vulnerable customers and customers that would have genuine difficulty paying, a wide range of methods for the repayment of charges associated with gas theft as an alternative to disconnection?

Question 5: Do you consider that Ofgem should include a licence requirement on all suppliers to establish a code of practice on, among other things, theft investigations and the detailed arrangements for compliance with our proposed consumer protection measures?

Question 6: Do you agree that our proposed new gas supply licence should be introduced as soon as reasonably practical?

CHAPTER: Four

Question 7: Have we correctly assessed the main impacts in the accompanying IA? Are there additional, material impacts that we should also consider?

Question 8: Do you agree with the assumptions that we have made and the outcome of our analysis in Appendix 2 of the accompanying IA?

Question 9: Which, if any, of the three proposals to increase theft detection should be implemented and why?

Question 10: Do you consider that there are any alternative proposals, or variations on existing proposals to improve theft detection that should be considered?

DRAFT IMPACT ASSESSMENT CHAPTER: Two

IA Question 1: What do you consider to be the scale of theft in the GB gas market? Do you consider that there is a material difference in the prevalence of gas theft between suppliers' customer portfolios? What factors drive any considered difference in theft distribution?

IA Question 2: Where theft has been detected, how long on average would you expect future revenues from a customer to fully reflect their consumption, ie what is

the expected reoffending rate over time. Do you expect there to be a material difference under each of the three proposals?

IA Question 3: For each industry proposal, are the proposed compliance measures sufficient to ensure suppliers conduct investigations to satisfactory standards and thereby protect customer interests? Are there any further measures that should be introduced to help address any perceived weakness?

DRAFT IMPACT ASSESSMENT CHAPTER: Three

IA Question 4: Are there any material differences between suppliers' ability to compete for incentive payments between UNC277 and UNC346? Would Enhanced SETS address any potential concerns raised about suppliers' ability to compete?

IA Question 5: Do you consider that the current NRPS proposal is likely to establish and realise targets for theft detection that are proportionate to the potential customer benefits? If not, what additional measures do you think are needed to meet this aim?

IA Question 6: Would the NRPS prevent some suppliers from realising additional commercial benefits from theft detection that may be available to them, eg by going further than the NRPS mandated investigation requirements? Would the focus of the NRPS proposals on data analysis reduce the overall efficiency of the market in theft detection by excluding investment in other sources of detection?

IA Question 7: For each of the three industry proposals, is a scheme necessary to compensate a supplier when it is not able to recover its costs from theft?

IA Question 8: Do you consider that cost and availability of services to support theft detection and investigation is a material issue for small suppliers?

DRAFT IMPACT ASSESSMENT CHAPTER: Four

IA Question 9: What percentage reduction in consumption would you expect customers to make when an illegal gas supply is detected? To what extent do you consider that this would result from a response to increased costs and/or an increased propensity to invest in energy efficiency measures?

DRAFT IMPACT ASSESSMENT CHAPTER: Five

IA Question 10: Do you have any further information on safety incidents where harm has directly resulted from theft of gas.

IA Question 11: Do you consider that any of the proposals are likely to reduce the health and safety of any particular individuals?

IA Question 12: Which proposal do you consider will have the greatest overall benefit on health and safety?

DRAFT IMPACT ASSESSMENT CHAPTER: Seven

IA Question 13: Do you consider that the proposed implementation timescales for each proposal are realistic and achievable. If not, what do you consider to be a realistic timeframe? What additional measures, if any, do you consider should be undertaken to secure implementation within a reasonable timeframe?

IA Question 14: Do you consider that gas transporters should be required to adhere to a code of practice on the conduct of theft investigations?

IA Question 15: What impact will either of the three industry proposals have on the annual number of investigations of theft in conveyance that gas transporters undertake and the total cost of undertaking these?

IA Question 16: What, if any, changes to the regulatory arrangements need to be made to enable gas transporters to adhere fully to their requirements to conduct theft investigations?

Appendix 2: Summary of questionnaire responses

1.1. In this appendix we present a summary of gas suppliers' responses to a questionnaire that we issued in December 2010. The purpose of the questionnaire, which was also issued to electricity suppliers as well as gas and electricity distribution companies, was to understand the current performance of the industry in tackling theft. Responses were received in January 2011.

1.2. The data request covered the period 2006 to 2010. In this Appendix we focus on the last two years covered by the questionnaire, 2009 and 2010, as data quality for the preceding years was poor from many suppliers⁶².

1.3. While for 2009 and 2010 the response rate⁶³ is more robust, responses were not received from all suppliers and suppliers did not provide data for all questions asked. This limits the potential conclusions that can be drawn from the data. To provide a measure of confidence in the aggregated data provided below each table includes the response rate for that specific question.

Suspected, investigated and identified theft

1.4. The sources of leads on gas theft varied significantly between suppliers. Table 1 below shows that there is no clear pattern and some suppliers have used the "other" category where they were not able to provide an accurate breakdown. The low figure for data analysis demonstrates that some suppliers are not proactive in theft detection. However, we consider that, in practice, this figure may be slightly higher as thefts generated by Revenue Protection Officers, and recorded under the "other" category will, to some extent, be data driven.

⁶² The majority of respondents indicated they were unable to retrieve the data requested in the questionnaire for the years 2006 to 2008.

⁶³ The response rate is a measure of the aggregate number of customers supplied by the suppliers that responded to a question divided by the total number of customers in that market.

Tackling gas theft

Table 1: Sources for theft detection (weighted average by number of theft cases found)

	Supplier 1	Supplier 2	Supplier 3	Supplier 4	Supplier 5	Average
Data Collector	22%	2%	0%	27%	22%	19%
MAM/MAP	3%	6%	0%	0%	0%	3%
GT/Xoserve	9%	91%	51%	28%	13%	20%
Analysis	12%	0%	0%	2%	15%	9%
Other*	54%	2%	49%	42%	21%	49%

* Revenue Protection Officer self-generated, tip-off, housing association, police, new tenant

1.5. Table 2 below reports the total number of suspected theft cases. This information is broken down by consumption category and, as expected, shows that the number of suspected cases is highest in the domestic SSP category⁶⁴.

Table 2: Suspected theft

	2009	2010	Response rate 2009	Response rate 2010
SSP – D	7,893	7,265	84%	84%
SSP – ND	575	493	67%	76%
LSP	647	683	62%	62%
Total	9,115	8,441		

1.6. Table 3 below shows that almost all reported suspected theft in 2009 and 2010 was followed up by an investigation⁶⁵ (respectively 98% and 96% of the suspected cases were investigated).

⁶⁴ In our tables, SSP – D refers to domestic sites in the SSP market and SSP – ND refers to non-domestic sites in the SSP market.

⁶⁵ These are investigations conducted after the ECV, where it is assumed that the case of theft falls under the responsibility of suppliers.

Table 3: Investigations after the ECV

	2009	2010	Response rate 2009	Response rate 2010
SSP – D	7,751	6,981	84%	84%
SSP – ND	518	430	67%	76%
LSP	638	677	62%	62%
Total	8,907	8,088		

1.7. Table 4 presents the number of cases of theft found by suppliers. This data relates to thefts after the ECV which are the suppliers' responsibility. The 8,907 investigations conducted in 2009 led to 2,933 theft cases being found, which represents a conversion rate of 33%. The conversion rate has improved slightly in 2010 to approximately 36%.

Table 4: Identified theft after the ECV

	2009	2010	Response rate 2009	Response rate 2010
SSP – D	2,567	2,443	100%	100%
SSP – ND	167	141	67%	76%
LSP	199	295	62%	62%
Total	2,933	2,879		

1.8. Table 5 reports suppliers' analysis on the estimated volume of gas abstracted from the thefts that they detected. The 2,879 cases of theft identified in 2010 lead to 53GWh of gas being illegally taken by customers. Given that the response rates for both questions are different it is not possible to provide an exact view on the average amount of gas taken per case of theft. However, our analysis estimates that this represents an average of 13,000kWh/year.

Table 5: Estimated volume of gas illegally taken (GWh/Year)

	2009	2010
Total	57.0	53.3
Response Rate	78%	75%

1.9. Table 6 below shows the average length of time that suppliers estimate that a theft has occurred when it is discovered. Suppliers have indicated that on average, theft by an SSP domestic customer occurs for approximately 2 years and 4 months. The length of theft is slightly higher for theft by SSP non-domestic customers, at around 2 years and 7 months, and also for theft by LSP customers, 2 years and 9 months.

Table 6: Average length of theft (Years)

	2006-2010	Response rate
SSP – D	2.3	67%
SSP – ND	2.6	67%
LSP	2.7	67%

Resources allocated to tackling theft across SSP and LSP sites

1.10. Suppliers have provided data on the human resources allocated to tackling gas theft. Table 7 shows the total number full time equivalents (FTEs)⁶⁶ across all suppliers that reported data for 2009 and 2010. One supplier accounts for approximately 85% of all FTEs (both in 2009 and 2010).

Table 7: FTEs allocated to tackling gas theft

	2009	2010
Total	83.3	91.3
Response rate	84%	84%

1.11. Table 8 presents the aggregate indirect costs⁶⁷ that suppliers have reported that they incurred in tackling theft of gas.

Table 8: Overhead costs with activities to tackle gas theft

	2009	2010
Total	£3,028,100	£3,707,998
Response rate	69%	69%

Costs of tackling theft

1.12. Table 9 shows the total reported retail value of the gas illegally taken. This value has increased in 2010, despite a slightly fewer number of cases of gas theft having been found that year and a lower volume of stolen gas being reported. It is unclear why this is the case.

Table 9: Retail value of the volume of gas illegally taken

	2009	2010
Total	£2,781,015	£3,722,420
Response rate	69%	69%

1.13. Table 10 shows that the costs incurred by suppliers with investigations have increased from £2m in 2009 to approximately £2.7m in 2010.

⁶⁶ FTE is a way to measure the resources allocated to a specific task or project. An FTE of 1.0 means that the person is equivalent to a full-time employee.

⁶⁷ These are the costs suppliers incurred in running the activities related with tackling theft of gas, but that are not directly linked to tackling specific theft cases. One example of an indirect cost is employee's salaries.

Table 10: Investigation costs

	2009	2010
Total	£2,000,393	2,697,064
Response rate	68%	68%

1.14. Table 11 shows the total costs incurred by suppliers from disconnection, reconnection and meter replacement costs associated with gas theft. It shows that suppliers have incurred additional costs of £375k with disconnecting, reconnecting, or replacing the meter when theft is found in 2009, and of £337k in 2010.

Table 11: Disconnection, reconnection and meter replacement costs

	2009	2010
Total	£375,042	£337,166
Response rate	61%	61%

1.15. Table 12 presents information about the number of warrants executed by suppliers. A supplier would apply to a magistrate or its equivalent in Scotland for a warrant which would grant rights of entry to inspect the premises and to disconnect supply where an offence has occurred. A warrant would be required where, for example, the customer did not allow access to a meter for inspection.

Table 12: Number of warrants

	2009	2010
Total	956	848
Response rate	50%	50%

1.16. Suppliers have also indicated that in 2010 they have successfully pursued one criminal conviction of a customer that had stolen gas. According to the information supplied provided by suppliers, no criminal convictions were conducted in 2009.

Benefits from tackling theft

1.17. Table 13 shows the aggregate recovered charges from customers (including charges for investigation and metering costs). Suppliers have indicated that this level of recovery represents about 60% of the amount billed to customers that have stolen gas (including the value of the gas and any investigation and meter disconnection, reconnection and exchange costs). However, the response rate for this question is low at around 57%. Further discussions with gas suppliers have led us to use a recovery rate of 25% for the SSP market and 60% for the LSP market in our draft IA.

Table 13: Revenue recovered from cases of theft

	2009	2010
Total	£1,652,485	£1,587,094
Response rate	57%	57%

Appendix 3: Draft proposals to amend the Gas Supply Licence

Condition [x]. Theft of gas

Objective

1.1 The objective of this licence condition (the “Objective”) is to ensure:

- (a) the licensee or any Representative takes all reasonable steps, individually and/or in cooperation with other licence holders where necessary, to:
 - (i) detect Theft of Gas;
 - (ii) investigate suspected Theft of Gas;
 - (iii) prevent Theft of Gas once detected;
 - (iv) prevent Theft of Gas by other means such as deterrence and the physical security of the supply in respect of any premises to which the licensee is registered for the purposes of the Network Code; and
- (b) the licensee’s or any Representative’s behaviour and actions towards its Customers when taking the steps mentioned in sub-paragraph 1.1(a) are conducted in a manner which is fair, transparent, not misleading, appropriate and professional.

1.2 The licensee must take all reasonable steps:

- (a) to secure the achievement of the Objective; and
- (b) to avoid doing anything which jeopardises its ability to achieve the Objective.

1.3 The steps which the licensee must take to secure the achievement of the Objective include, without limitation, the steps which are detailed at paragraphs 1.5 to 1.14 of this condition, the obligations set out in paragraphs 3 and 4 of standard condition 17 and paragraph 6(e) of standard condition 30.

1.4 For the avoidance of doubt, where the licensee is not registered at a premises for the purposes of the Network Code, its obligations under paragraphs 1.1 and 1.2 are limited to the provision of notification to the Relevant Gas Transporter under paragraphs 3 and/or 4 of standard condition 17.

Requirement to detect, prevent and investigate theft of gas and damage

1.5 In respect of any premises to which the licensee is registered for the purposes of the Network Code, the licensee or any Representative must take all reasonable steps to detect and prevent Theft of Gas.

1.6 Where, in respect of any premises to which the licensee is registered for the purposes of the Network Code, the licensee or any Representative has reasonable grounds to suspect Theft of Gas, it must take all reasonable steps to fully investigate that suspected Theft of Gas.

1.7 Paragraph 1.6 does not apply if the Gas Transporter is required to investigate whether the supply of gas is/was illegally taken under paragraphs 1 and 2 of standard condition 7 of the Gas Transporter Licence.

The Theft Arrangement

1.8 The licensee must be a party to, comply with, and maintain such arrangement to give effect to the Objective, as the Authority may direct (the "Theft Arrangement").

1.9 The licensee must, take such steps as are necessary and within its reasonable control, and not take any unreasonable steps to prevent or delay, to ensure that the Theft Arrangement is implemented by no later than [xx] months after this condition takes effect (or such later date as the Authority may direct).

1.10 The licensee must take all reasonable steps to secure and implement changes to the Theft Arrangement and its systems, procedures and processes which are necessary to give full, timely and practical effect to the Theft Arrangement.

1.11 The licensee must take all reasonable steps to cooperate with other licence holders where necessary, to facilitate the achievement of the Theft Arrangement.

Standards for theft of gas investigations

1.12 The licensee must ensure that the following standards are met when it is taking any of the steps referred to in paragraphs 1.1, 1.2, 1.3 and 1.4 of this Condition:

Tackling gas theft

- (a) The licensee or any Representative must take all reasonable steps to identify whether the Domestic Customer and/or the occupants of the Domestic Premises (in this condition “the relevant premises”) is of Pensionable Age, disabled or chronically sick;
- (b) The licensee or any Representative must take all reasonable steps to identify whether a Domestic Customer at the relevant premises will have difficulty in paying all or part of the Charges for the Supply of Gas resulting from Theft of Gas;
- (c) Where the licensee or any Representative knows or has reasons to believe that a Domestic Customer and/or the occupants of the relevant premises is of Pensionable Age, disabled or chronically sick the licensee or any Representatives must take all reasonable steps not to stop the supply of gas to the relevant premises in Winter;
- (d) Where the licensee or any Representative has identified a Domestic Customer and/or the occupants of the relevant premises is reasonably suspected to be of Pensionable Age, disabled or chronically sick and/or the Domestic Customer at the relevant premises will have difficulty in paying all or part of the Charges for the Supply of Gas resulting from Theft of Gas, the licensee or any Representative must, prior to stopping the supply of gas to the relevant premises, at a minimum offer and facilitate for the Domestic Customer to pay those Charges for the Supply of Gas by using a Prepayment Meter, where it is safe and reasonably practicable in all the circumstances of the case for the Domestic Customer to do so;
- (e) The licensee or any Representative must have sufficient evidence to establish (on the balance of probabilities) the Statutory Disconnection Power before stopping the supply of gas to a premises on grounds of Theft of Gas;
- (f) The licensee or any Representative must have sufficient evidence to establish (on the balance of probabilities) that Theft of Gas has occurred before requiring payment of all or part of the Charges for the Supply of Gas relating to that Theft of Gas; and
- (g) The licensee or any Representative must provide clear, timely and accurate information and advice to the Customer about:
 - (i) the basis any assessment made by the licensee that Theft of Gas has been committed;
 - (ii) the basis for the calculation of any Charges for the Supply of Gas associated with the Theft of Gas made to the Customer;



Tackling gas theft

- (iii) what steps the Customer should take if they wish to dispute that a Theft of Gas had occurred; and
- (iv) the steps a Customer may take to reinstate supply once the licensee has exercised the Statutory Disconnection Power.

1.13 The licensee and/or any Representative must keep a record of its compliance with its obligation under this licence condition.

1.14 The licensee must take all reasonable steps to establish management arrangements that facilitate the licensee’s compliance with its obligations under this condition, including, as appropriate, steps to ensure that any agents and subcontractors of the licensee establish equivalent arrangements.

Definitions for Condition

1.15 In this condition:

Theft of Gas	includes, but is not limited to; (a) circumstances described in paragraphs 10(1)(a) and 11(2) of Schedule 2B to the Gas Act 1986 in so far as they relate to a gas supplier; and (b) circumstances described in paragraphs 10(1)(b) and 10(1)(c) of Schedule 2B to the Gas Act 1986.
Statutory Disconnection Power	means paragraphs 10(2) and 11(2)(b) of Schedule 2B to the Gas Act 1986

[Introduce new paragraph after SLC 30.6(d)]

The Theft of Gas Customer Code of Practice

30.6 The relevant objectives referred to in sub-paragraph 30(a) are:

- (e) securing compliance with standard condition [state number] Theft of gas.



Tackling gas theft

[Introduce new paragraph after SLC27.11A]

27.12 The prohibitions described in paragraphs 27.9 to 27.11 shall not apply where the licensee is considering exercising its Statutory Disconnection Power.

[Introduce additional definition after SLC27.16]

Statutory Disconnection Power	means paragraphs 10(2) and 11(2)(b) of Schedule 2B to the Gas Act 1986
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Appendix 4: Glossary

A

Annual Quantity (AQ)

The sum (measured in kWh or therms) of the annual consumption of all meters on a site. AQs are based on historical usage from previous years.

Allocation of Unidentified Gas Expert (AUGE)

An independent expert to determine a methodology for the allocation of unallocated gas, to be appointed under the terms of UNC Modification Proposal 229.

AQ Review

A review of the User's determination of the AQ in respect of a Supply Meter Point.

C

Central Revenue Protection Unit (CRPU)

The CRPU is part of the Enhanced SETS proposal. The role of the CRPU would be to enter the market to offer services to suppliers to help them respond to the incentive scheme set up under SETS.

Customers

Parties who have a contract with a supplier to take gas at a Supply Point.

D

Daily Metered (DM) Supply Points

Supply points that have annual gas consumption greater than 58,600,000KWh. DM Supply Points are equipped with mandatory telemeter equipment, such as a datalogger. Any supply point which is directly connected to the NTS will also be daily metered.

Distribution Connection and Use of System Agreement (DCUSA)

A multi-party contract between the licensed electricity distributors, suppliers and generators of Great Britain. It is concerned with the use of the electricity distribution systems to transport electricity to or from connections to them.

E

Emergency Control Valve (ECV)

A valve which limits the supply of gas to an individual Supply Point.

Enhanced SETS

Enhanced SETS builds on the SETS proposal to increase theft detection. In addition to a code of practice on theft investigations it would add the RPACA and may also add the CRPU.

G

Gas Distribution Network (GDN)

A network through which gas is taken from the high pressure transmission system and distributed through low pressure networks of pipes to industrial complexes, offices and homes. There are eight GDNs in Britain, each covering a separate geographical region.

Gas Transporters (GTs)

Holders of a licence to operate a system to convey gas granted under section 7 paragraph 4 of the Gas Act 1986 as amended.

I

Independent Gas Transporter (IGT)

An operator of a small local gas network, most of which are being built to serve new housing. IGTs may levy transportation charges on shippers.

L

Larger Supply Point (LSP)

A meter point with an annual consumption greater than 73,200kWh (2,500 therms).

N

National Revenue Protection Service (NRPS)

Proposal to increase theft detection by establishing a central database to profile theft risk at each supply point. It would require the highest risk cases to be investigated by suppliers.

R

Revenue Protection Activity Co-ordination Agent (RPACA)

The RPACA is part of the Enhanced SETS proposal. It would provide services (such as management information and a telephone tip-off line) that may not be provided to the same extent in a competitive market.

S

Supplier Energy Theft Scheme (SETS)

A proposal to increase theft detection by introducing incentives on shippers. It would be implemented through either UNC277 or UNC346.

Supply Point Administration Agreement (SPAA)

A multi-party agreement to which all domestic gas suppliers and all gas transporters are required by their licences to accede. It sets out the inter-operational arrangements between gas suppliers and transporters in the GB retail market.

Shipper

An agent who arranges for the conveyance of gas over the distribution network to final consumers. Shippers pay transportation charges to the relevant gas transporter and are holders of a licence given under Section 7A (2) of the Gas Act 1986 as amended.

Smaller Supply Point (SSP)

An SSP is a supply point with an annual consumption of less than 73,200kWh (2,500 therms).

Supplier

Holders of a licence to supply gas given under Section 7A (1) of the Gas Act 1986 as amended or a person excepted from the requirement to hold a licence by virtue of paragraph 5 of schedule 2A of the Act.

Supply Meter Point (SP)

A point at which consumers take gas off the gas transporter's network.

T

Theft of gas

Describes a number of offences under schedule 2B of the Gas Act 1986 where a customer prevents a meter from correctly registering the amount of gas supplied, has damaged equipment or reconnects the supply without the relevant permission.

U

Unallocated Gas

Gas which is offtaken from a gas transporters network without being charged to any one shipper.

Uniform Network Code (UNC)

The contractual framework for the NTS, GDNs and shipper.

X

xoserve

A joint venture delivering transportation transactional services, owned by the five large gas transporters and the transmission operator.

Appendix 5: Feedback questionnaire

1.1. Ofgem considers that consultation is at the heart of good policy development. We are keen to consider any comments or complaints about the manner in which this consultation has been conducted. In any case we would be keen to get your answers to the following questions:

1. Do you have any comments about the overall process, which was adopted for this consultation?
2. Do you have any comments about the overall tone and content of the report?
3. Was the report easy to read and understand, could it have been better written?
4. To what extent did the report's conclusions provide a balanced view?
5. To what extent did the report make reasoned recommendations for improvement?
6. Do you have any further comments?

1.2. Please send your comments to:

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