

By email to [smartermarkets@ofgem.gov.uk](mailto:smartermarkets@ofgem.gov.uk)

Chiara Redaelli  
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Ofgem  
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SW1P 3GE

28 August 2013

Dear Chiara,

**ELEXON's response to 'Tackling Electricity Theft – Consultation and Draft Impact Assessment'**

We welcome the opportunity to provide ELEXON Limited's views on the above consultation and Draft Impact Assessment published by Ofgem on 3 July 2013.

The views expressed in this response are those of ELEXON Limited alone, and do not seek to represent those of the Parties to the BSC.

We confirm that this letter and its attachment may be published on Ofgem's website.

We would be happy to discuss our response with you, in particular to explore our response to questions 5 and 8 of the main consultation.

If you or your colleagues need anything further from ELEXON, please contact me on 020 7380 4313 or by email: [jon.spence@elxon.co.uk](mailto:jon.spence@elxon.co.uk).

Yours sincerely

Jon Spence  
Senior Market Advisor

# Tackling electricity theft – Consultation

## Chapter Three

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

Yes, we believe new licence obligations in relation to theft are appropriate.

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

Yes, we believe Appendix 3 reflects the policy intent.

### **Question 3: Do you consider that electricity suppliers should be required to offer vulnerable customers and customers that would have genuine difficulty paying, different methods for the repayment of charges associated with electricity theft as an alternative to disconnection?**

We believe this is a matter for electricity Suppliers and have no view.

### **Question 4: Do you agree that our proposed new electricity supply licence conditions should be introduced as soon as reasonably practical?**

Yes, we believe it is appropriate to introduce the new licence conditions as soon as possible to provide certainty around obligations and encourage the tackling of theft.

## Chapter Five

### **Question 5: Do you agree with our approach to conducting the draft IA, the assumptions that we have made and the outcome of our analysis in the accompanying draft IA?**

Whilst we agree generally with the approach to conducting the draft IA and the assumptions made, we have reservations about the practicalities of combining enhanced audit, Settlement-cost sharing and a detection/volume incentive schemes. Under the current Settlement arrangements, energy can either be allocated to a Supplier or 'smeared' (as unallocated energy) across all Suppliers via GSP Group Correction. It is currently not possible to allocate 100% of detected stolen units to Suppliers (for the purposes of supporting an incentive scheme), whilst at the same time distributing 80% of the liabilities from the entry of unrecorded units to all Suppliers (for the purposes of Settlement). This artificial allocation of units is likely to have impacts on Suppliers' trading positions.

ELEXON has previously discussed with industry how to allocate lost energy arising from the identification

of theft. As part of [Standing Modification Issue 39](#) ('Unrecorded Units identified by Revenue Protection Services'), we considered an option whereby all stolen units were shared across the Supplier community via GSP Group Correction (i.e. with no requirement to account for these units), thus removing the Settlement disincentive. Detected stolen units would be reported under a separate mechanism (out-with the Settlement systems) for the purposes of DUoS billing and the Distribution Price Control Review (the latter requirement being no longer applicable). This would help reduce the overall volume of theft, but at the expense of the accurate allocation of detected stolen units. Tracking units in the Settlement systems for the purposes of an incentive scheme, whilst excluding a proportion of those units from Suppliers' allocated units, would incur much higher costs than the indicative values estimated for Option 3 in the Issue 39 documentation. The likely costs would be closer to, and probably exceed those for Option 2 in the Issue 39 documentation. An incentive scheme (detection and/or volume) could presumably achieve the same results with or without Settlement-cost sharing, subject to appropriate calibration of the incentive payments?

**Question 6: Have we correctly assessed the main impacts in the accompanying draft IA? Are there additional impacts that we should consider?**

Yes. The impacts identified in the draft IA appear comprehensive.

**Question 7: Which, if any, of the proposed policy measures (or package of policy measures) to support theft investigation, detection and prevention should be implemented and why?**

ELEXON has identified a need for enhanced audit and performance assurance of the Settlement arrangements. We believe that there are a number of ways in which this can be achieved (as discussed by the Standing Modification Issue 39 group and in our response to question 8 below). In order to ensure that changes to Settlement systems are efficient and cost-effective, we need to know what incentive mechanisms the Settlement data will need to support. We are open-minded about which of the incentives should be implemented (subject to our reservations in response to question 5 above).

**Question 8: Do you consider that there are alternative proposals, or variations of the combinations of the proposed policy measures that should be considered?**

Yes.

Table 8 in Appendix 2 of the consultation document shows the average length of theft as 1.4 years for Non Half Hourly metered (domestic and non-domestic) customers. The impact assessment uses average durations of 12, 24 and 36 months in the input data to the model. Given the average duration of the theft instance itself (plus the time taken to confirm that theft has occurred, to establish or estimate the number of units stolen and to submit these to Settlement), it is likely that the Final Reconciliation Run will have taken place (at about 14 months) in respect of some of the dates affected. This means that the longer it takes to confirm that a theft has occurred and to determine the unallocated units, the greater the number of units that will be 'timed out' from the Reconciliation calculations. It would be possible, though not desirable, to allocate the unrecorded units to periods other than those in which they were taken. Otherwise any units consumed for dates earlier than 14 months before each Reconciliation Run, could only be accounted for by an authorised Trading Dispute. Trading Disputes are optional and Suppliers are not incentivised to raise them in these circumstances. As such, it would be worth

considering removing the Settlement requirement to account for unallocated units as part of the Reconciliation runs, and introducing a process (akin to the current Extra Settlement Determination process) whereby a Settlement adjustment is made outside the Settlement and Reconciliation processes (and in longer timescales) to account for unrecorded units. Such an application, which could still form part of BSC governance, would also support any proposed incentive mechanisms.

We note Paragraph 4.19 of the consultation, which states that the TRAS could be given the responsibility for maintaining records of units entering settlement. Subject to Modification, BSC central systems would hold revenue protection adjustments. To aid efficiency and achieve further value from existing infrastructure, the BSC systems could be extended to maintain these records of settlement units and in addition perform calculation and administration of incentive payments. These would draw upon the ready availability of market share data and proven fund clearance functions that ELEXON undertakes for administration of the BSC. We would be happy to discuss this option with Ofgem further.

## Chapter Six

### **Question 9: Do you agree with our view that DNOs, for the time being, should not be included in an incentive scheme?**

No. We wonder if the DNOs can be incentivised to address theft in conveyance?

The various incentive schemes for Suppliers are reliant to varying degrees on evidence that estimates of stolen units have been entered into Settlement. There is no mechanism within the current Settlement arrangements for separately identifying volumes of theft in conveyance. We would welcome any initiatives that reduce the number of units subject to GSP Group Correction, but are open-minded on how this is best achieved in respect of theft in conveyance. Any information about the extent to which theft in conveyance is contributing to GSP Group Correction would be helpful (by a process of elimination) in understanding other causes of GSP Group Correction.

### **Question 10: Do you agree with our view that DNOs should have licence obligations to tackle theft in conveyance?**

Yes, see our response to Question 9.

### **Question 11: Are you aware of any alternative proposals to support DNOs in tackling theft in conveyance that should be considered? If so, please provide further details.**

No

For more information on our response, please contact:

*Jon Spence, Senior Market Advisor*

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# Electricity theft – Draft Impact Assessment

## Chapter Two

### **IA Question 1: Do you consider we have captured all relevant actions that, if undertaken by suppliers, can contribute to tackling electricity theft?**

Yes. There is a recognised weakness in the Settlement audit arrangements in terms of ensuring that detected stolen units are accounted for accurately. This is considered to be one of the 'top Settlement Risks', as noted in paragraph 2.33 of the consultation document. This needs to be addressed by enhanced audit and performance of the Settlement process for theft-related units and we agree that this measure is not necessarily conditional on the various theft-incentive measures being considered. However, the improved tracking of detected stolen units in Settlement would be required to support the theft-incentive measures, so we strongly agree with the view in 1.27 that enhanced audit and incentive measures are best developed in parallel.

### **IA Question 2: Do you consider our approach to the draft IA suitable for demonstrating the current commercial disincentives and challenges suppliers face to tackle theft? If not, what alternative approach would you suggest to be best?**

Yes.

## Chapter Three

### **IA Question 3: What do you consider to be the scale of theft in the GB electricity market?**

We have no metrics.

### **IA Question 4: Do you consider that there is material difference in the prevalence of electricity theft between suppliers' customer portfolio? What factors drive any considered difference in theft distribution?**

Table 5 in Appendix 2 of the consultation document shows that instances of theft among Half Hourly metered customers are rare. This could create a risk that 'niche' Suppliers with predominantly Half Hourly metered (and larger non-domestic Non Half Hourly metered customers) subsidise the detection of theft disproportionately under the incentive schemes.

### **IA Question 5: When theft has been detected, what actions do you take to ensure accurate estimates of the volume stolen and to ensure stolen units are entered into settlement?**

There is a recognised need to clarify the requirements for entering stolen units into Settlement. This is dependent to an extent on what mechanism is needed to track these units through the Settlement processes. This, in turn, is dependent on what incentive schemes the Settlement processes will need to

support.

**IA Question 6: What is your estimate of the re-offending rates? Are there any actions you take to prevent re-offence at a premise where theft is detected?**

We have no metrics.

**IA Question 7: For each incentive measures, are the proposed compliance measures sufficient to ensure suppliers conduct investigations to satisfactory standards and thereby protect consumer interests? In addition to the proposed new Revenue Protection Code of Practice on theft investigation being developed under the DCUSA, are there any further measures that should be introduced to help address any perceived weakness?**

We believe this is a matter for electricity Suppliers and have no view.

#### **Chapter Four**

**IA Question 8: Do you consider the incentive problem described in the consultation to be a reasonable representation of the issues and challenges suppliers face to tackle theft?**

Yes.

**IA Question 9: To what extent do you consider the detection-based and the volume-based incentive schemes are likely to establish and realise targets for theft detection that are proportionate to the potential consumer benefits? Do you have any views on the two variations (cap / no cap) of each of those incentives schemes?**

Assuming that theft instances are a mixture of high-number / low-volume (household) and low-number / high-volume (cannabis farms etc), a combination of detection-based and volume-based incentive schemes are probably required to target both categories of theft. There is a risk that setting incentive payments below wholesale prices would offer insufficient incentive. Conversely, setting incentive payments above wholesale prices could act as a perverse incentive to overstate stolen volumes, without suitable controls.

Limiting the funds available to Suppliers via an incentive pot could have an undesired 'dampening' effect, whereby Suppliers are reluctant to commit resources to theft detection because of uncertainty about the value of the reward.

**IA Question 10: Do you consider that the cost-sharing mechanism could address the disincentive suppliers face to enter estimated stolen units into settlement?**

Reducing Settlement liabilities and making an incentive payment appear to achieve the same end. Tackling the problem from both ends introduces additional complexity in terms of calibrating a scheme(s) and a greater risk of getting the calibration wrong. It would also come at a higher cost in terms of changes to Settlement systems, given that the current systems would not allow 100% allocation for the purposes of an incentive scheme, but only 20% for the purposes of calculating Supplier

volumes.

**IA Question 11: Do you consider that additional or alternative measures to the three incentive measures, to the enhance audit and to the TRAS are needed to address the incentive problem and improve theft investigation, detection and prevention?**

The measures identified are good starting point in terms of addressing the incentive problem and the TRAS should improve theft investigation and detection.

**IA Question 12: Do you consider that the cost and availability of services to support theft detection and investigation is a material issue for small suppliers?**

We have no views on Questions 12 to 17.

### Chapter Five

**IA Question 13: Do you agree with our initial views on consumer behaviour in respect of energy efficiency?**

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**IA Question 14: What percentage reduction in consumption would you expect customers to make when an illegal electricity 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?**

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### Chapter Six

**IA Question 15: Do you consider the proposed incentive measures would have any direct or indirect impacts on health and safety others than the areas discussed in this draft IA?**

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**IA Question 16: What incentive measure (or combination of incentive measures) do you consider would have the greatest impact on health and safety?**

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### Chapter Seven

**IA Question 17: Do you consider there are other risks or unintended consequences of the proposed policy measures not discussed in this draft IA? What alternative policy measures do you consider could address these risks?**

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### Chapter Eight

**IA Question 18: Do you consider that the implementation timescale for our proposals is 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?**

Changes to Supplier, Supplier Agent and central Settlement systems and processes will be required to deliver enhanced audit and to support any incentive schemes. The extent of these changes will depend on the incentive scheme(s) selected. The impact assessments of the high level options considered under Issue 39 suggested implementation timescales of 6 to 12 months for Suppliers and Supplier Agents and 10 months for central systems (if end-to-end tracking of revenue protection adjustments is required). Agreement about incentive schemes would be needed by Q1 2014 in order to put these schemes in place ahead of the planned implementation of the TRAS in Q1 2015.

**IA Question 19: Do you consider that our approach to enhancing obligations on DNOs would provide more focussed action on tackling theft in conveyance? If not, what do you consider to be an alternative approach?**

We have no views on question 19.

For more information on our response, please contact:

*Jon Spence, Senior Market Advisor*

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