

Modification proposal:	Distribution Connection and Use of System Agreement (DCUSA) DCP288, DCP288A, and DCP288B – Introduction of the Electricity Theft Detection Incentive Scheme		
Decision:	The Authority ¹ directs that modification ² DCP288 be made ³		
Target audience:	DCUSA Panel, Parties to the DCUSA and other interested parties		
Date of publication:	4 May 2018	Implementation date:	5 Working Days After Authority Decision

Background

The theft of electricity increases the prices for consumers and reduces safety. It leads to a misallocation of costs among suppliers, which can distort competition and hamper the efficient functioning of the market. In March 2014, we published our decision on the new arrangements for tackling electricity theft alongside an impact assessment. We set out the principles for a theft detection incentive scheme as part of our final proposals and we considered that they should be implemented through industry code governance.⁴

The modification proposal

DCP288: British Gas raised DCP288 to introduce a theft detection incentive scheme within the DCUSA, in line with the principles we set out in our final proposals and to better facilitate DCUSA Objective (b). The proposed electricity incentive scheme is based on the Gas Theft Detection Incentive Scheme (GTDIS) approved under SPAA CP 14/268 and the amendments made via CP 16/327.⁵ The GTDIS went live on 1 June 2017. DCP288 has been raised to introduce a scheme for the electricity market that the proposer considers is equivalent to the one in gas. The mechanics of the incentive scheme are set out in full in the legal text accompanying DCP288 and are summarised below.

Targets

DCP288 proposes that an overall theft target would be published before the beginning of each year. This target would then be split between domestic and commercial sectors, providing sector targets for each. In the first year of the scheme the theft target would be based upon the assumptions set out⁶ in the Final Impact Assessment⁷ published alongside our Tackling Electricity Theft Final proposals. The target in the first year is 34,000 Confirmed Theft detections, with a breakdown of 30,000 thefts in the domestic sector and 4,000 thefts in the commercial sector. In the second year the Theft Target split by sector would be the same as the first year, unless there is sufficient data for the scheme administrator to complete a review of the methodology. Individual supplier targets would be based on market shares.

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

² 'Change' and 'modification' are used interchangeably in this document.

³ This document is notice of the reasons for this decision as required by section 49A of the Electricity Act 1989.

⁴ Tackling Electricity Theft: New requirements for gas suppliers – Decision Document. Ofgem Ref 137/12. See: <https://www.ofgem.gov.uk/publications-and-updates/tackling-electricity-theft-%E2%80%93-way-forward-0>

⁵ CP14/268: https://www.ofgem.gov.uk/sites/default/files/docs/2015/10/cp14-268d_0.pdf, CP16/327: <https://www.ofgem.gov.uk/publications-and-updates/supply-point-administration-agreement-change-proposals-cp16327-revision-and-implementation-gas-theft-detection-incentive-scheme-and-cp16337-movement-leads-based-theft-incentive-scheme>

⁶ The Ofgem Impact Assessment was carried out in 2014. Since then the market has grown and more Suppliers have joined the industry. The TIG agreed to increase the domestic theft target. The size of the commercial theft target had been due to the inclusion of cannabis farms within the Incentive Scheme calculation. The TIG agreed to remove this from commercial theft target as cannabis farms.

⁷ https://www.ofgem.gov.uk/sites/default/files/docs/2014/03/electricitytheft-iafinal_0.pdf

Incentive payments and pot

The proposed Theft Detection Value is the incentive payment for each theft detection. In the first year this would be set at £400 per confirmed theft detection for both sectors. After the first two years, the scheme administrator would be responsible for adjusting the Theft Detection Value in line with the Consumer Price Index (CPI) or by another methodology established by the Panel. There would also be a requirement for the scheme administrator to establish the split between the consumer and commercial sectors. There would be individual incentive pots for the domestic and commercial sectors, and each year these would be calculated based on the sector theft target and the Theft Detection Value.

Reporting

Qualifying Suppliers⁸ would continue to submit data as currently required under the Theft Risk Assessment Service Arrangements. A monthly indicative summary report would detail an aggregate level number of confirmed thefts of each supplier against their target in each of the sectors. A final report would be produced after the scheme year, and the scheme administrator would use this to calculate the financial debits and credits.

DCP288A: First Utility raised an alternative proposal on 14 April 2017. The overall mechanics of this alternative are similar to DCP288, however it proposes a different approach to calculating the theft target for smaller suppliers. Under DCP288A, the theft target for suppliers with less than 2 million electricity metering points would be an adjusted percentage in the first two years of the scheme.⁹ The shortfall would be allocated to suppliers with more than 2 million electricity points, in addition to their market share derived percentage allocation. DCP288A aims to provide a 'softer landing' for smaller and mid-tier suppliers.

DCP288B: Gazprom Marketing and Trading Retail Limited raised CP288B on 25 July 2017. DCP288B proposes a scheme based upon the investigation of received leads and Theft Risk Assessment Service (TRAS) Qualified Outliers, rather than on the absolute detection of confirmed theft. The incentive scheme proposed by DCP288 and DCP288A would reward suppliers only where actual theft is detected. An underlying assumption of DCP288/288A is that theft is broadly consistent across the whole market. Therefore, each supplier has within its portfolio instances of theft that are proportionate to its total market share.

Like DCP288 and DCP288A, DCP288B proposes the overall incentive pot split by domestic and commercial sectors; but it does not propose individual supplier targets and instead aims to incentivise each supplier to investigate all leads provided by the TRAS service provider or an Electricity Distribution Network Operator. The incentive pots in year 1 would be set to the same value as in DCP288 but in future years would be based on the number of completed investigations in each sector in the previous year, the investigation completion value for that year, and any money rolled over from the previous year. Investigations concluded within 90 working days would qualify for an incentive payment. This would be set at £400 per completed investigation in year 1 and then, as in DCP288, adjusted by the scheme administrator. Financial debits and credits would be based on the total number of investigations completed in the timeframe resulting from the qualified outliers and leads.

⁸ A Qualifying Supplier Party is a supplier that has been active in the market throughout the whole Scheme Year and may include suppliers whose target is less than one, that elects to be part of the scheme.

⁹ In year 1 the adjustment percentage will start at 33.3% of the suppliers confirmed theft target, increasing to 66.6% in year 2, and reaching 100% in year 3.

DCUSA Parties' recommendation

DCP288, 288A, 288B were issued to parties for voting on 19 January 2018. The recommended implementation date for DCP 288, 288A or 288B is 5 working days after the Authority Decision, and the scheme start date for them all is the 1 June 2018.

DCP288: In each party category where votes were cast there was majority (>50%) support for the proposal and for its proposed implementation date. In accordance with the weighted vote procedure, the recommendation to the Authority is that DCP288, and its proposed implementation date, is accepted.

DCP288A: In each party category where votes were cast there was less than majority (<50%) support for the proposal and for its proposed implementation date. In accordance with the weighted vote procedure, the recommendation to the Authority is that DCP288A is rejected.

DCP288B: In each party category where votes were cast there was less than majority (<50%) support for the proposal and for its proposed implementation date. In accordance with the weighted vote procedure, the recommendation to the Authority is that DCP288B is rejected. The outcome of the weighted vote is set out in the table below:

DCP288	WEIGHTED VOTING (%)							
	DNO ¹⁰		IDNO/OTSO ¹¹		SUPPLIER		DG ¹²	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	n/a	n/a	n/a	n/a	74%	26%	n/a	n/a
IMPLEMENTATION DATE	n/a	n/a	n/a	n/a	80%	0%	n/a	n/a

DCP288A	WEIGHTED VOTING (%)							
	DNO		IDNO/OTSO		SUPPLIER		DG	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	n/a	n/a	n/a	n/a	4%	96%	n/a	n/a
IMPLEMENTATION DATE	n/a	n/a	n/a	n/a	80%	0%	n/a	n/a

DCP288B	WEIGHTED VOTING (%)							
	DNO		IDNO/OTSO		SUPPLIER		DG	
	Accept	Reject	Accept	Reject	Accept	Reject	Accept	Reject
CHANGE SOLUTION	n/a	n/a	n/a	n/a	6%	94%	n/a	n/a
IMPLEMENTATION DATE	n/a	n/a	n/a	n/a	80%	0%	n/a	n/a

Our decision

We have considered the issues raised by the proposal, the Change Declaration and Change Report submitted to us on 13 February 2018.¹³ We have considered and taken into account the vote of the DCUSA Parties on the proposal which is attached to the Change Declaration. We have concluded that:

- implementation of **DCP288** will better facilitate the achievement of the Applicable DCUSA objectives;¹⁴ and
- directing that the modification is approved is consistent with our principal objective and statutory duties.¹⁵

¹⁰ Distribution Network Operator

¹¹ Independent Distribution Network Operator/Offshore Transmission System Operator

¹² Distributed Generation

¹³ Available from the DCUSA website: <https://www.dcusa.co.uk/SitePages/Activities/Change-Proposal-Register.aspx>

¹⁴ The Applicable DCUSA Objectives are set out in Standard Licence Condition 22.2 of the Electricity Distribution Licence.

¹⁵ The Authority's statutory duties are wider than matters that the Parties must take into consideration and are detailed mainly in the Electricity Act 1989 as amended.

Reasons for our decision

We agree with the proposers and the Panel that DCP288, 288A, and 288B should be assessed against DCUSA objective (b) and that each has a neutral impact on the other applicable objectives.

Applicable DCUSA Objective (b)– the facilitation of effective competition in the generation and supply of electricity and (so far as is consistent with that) the promotion of such competition in the sale, distribution and purchase of electricity

DCP288

The proposer's view is that DCP288 will provide suppliers with a commercial incentive to identify theft in their portfolio. The majority of suppliers share the view that objective (b) is better facilitated as it should improve the misallocation of costs among suppliers, which can distort competition and hamper the efficient functioning of the market. A number of suppliers were supportive of having similar schemes for gas and electricity.

A number of suppliers disagreed that DCP288 better facilitated objective (b). They challenge the assumption that theft is evenly distributed across the market. Their view is that if the scheme is based on the number of detected thefts rather than the number of investigations this could mean that some parties could be unduly penalised, despite undertaking extensive investigations. They are concerned there is a risk the scheme creates a cross-subsidy and distorts competition, and that a one size fits all approach across the industry could be unfair on smaller players.

DCP288 builds upon the analysis and impact assessment that we undertook in our tackling electricity theft proposals. We agree that overall DCP288 better facilitates objective (b) as it should provide a greater incentive to detect theft over and above the volumes that would be detected without a scheme. We understand the concerns regarding the risk of a cross-subsidy but in the absence of evidence on the materiality we feel a scheme designed along the principles set out in our tackling theft work would better reduce the overall industry level of theft, and this would be of benefit to consumers and competition. The principles that we set out in our tackling electricity theft work were based on a substantive amount of analysis, where we concluded an incentive scheme that was based on the outcome of detected theft was appropriate.

DCP288A

The proposer's rationale for the alternative modification is based on the view that consumers switching to smaller suppliers and fixed tariffs are less likely to engage in energy theft. The adjusted target for suppliers with under 2 million metering points is aimed at providing smaller and mid-tier suppliers a softer landing.

Other suppliers argue that consumers engaging in theft may switch from large to small suppliers to avoid detection, once they know they are under investigation. One supplier's view was that suppliers in the market do not need a soft landing, as they should already have in place adequate provisions for investigating theft in line with their licence obligations. Another supplier questioned whether a relaxed theft target for smaller suppliers would facilitate effective competition between suppliers.

We agree that suppliers all have licence obligations to detect, investigate and prevent theft. We published our tackling theft proposals and the principles for a theft incentive scheme in 2014 and agree that suppliers should have had sufficient time to put suitable arrangements in place. No evidence has been provided to support the proposed 2 million metering point threshold or that small supplier customers attempt theft less. In the

absence of further evidence we see no basis for providing further exceptions to the existing one for small suppliers with a theft target less than 1, which can decide whether to opt into the scheme.

DCP288B

The proposer of DCP288B is seeking to mitigate the risk of cross subsidy from suppliers that have a smaller proportion of theft in their portfolio relative to their market share to those that have a larger proportion, which they consider may distort the market and competition. A number of suppliers supported the view that the underlying assumption in DCP288, that theft is evenly distributed, is wrong.

One supplier highlighted that the proposer of DCP288B has not provided any additional evidence to support the proposal, and that the theft target proposed under the scheme is only a small proportion of the actual level of theft taking place. A few suppliers were concerned that the scheme might incentivise focus on lower quality, and less reliable theft leads to qualify for the incentive payments. There were also concerns regarding what constitutes an investigation, ie a physical site visit or desk research. The panel has been given the right to carry out audits of any supplier's evidence for completed investigations.

We have similar concerns to those raised regarding whether the scheme would clearly provide an incentive to detect theft at a level that is beneficial for consumers, and whether suppliers may focus on volume of investigations rather than targeting resources appropriately. This could lead to a large number of low quality investigations that suppliers are rewarded for, but little change in the actual volume of thefts detected. We have some sympathy with the issue DCP288B is seeking to tackle but on balance think that DCP288 will better tackle an industry level of theft. DCP288 is based on principles arrived at after a substantive amount of work looking into electricity theft and an impact assessment. An incentive scheme based on the outcome we are seeking to achieve, an increase in the detection of theft and reduction in the level of theft, is both appropriate and supported by extensive evidence and analysis carried out as part of our tackling electricity theft work. We are open to considering alternative schemes however, this will need to be assessed in light of new evidence and analysis.

Conclusion

Our view is that a theft incentive scheme is a proportionate measure to mitigate the risks, and it would be better to implement a scheme and review it overtime as evidence of any issues arise. We agree with the recommendation of the panel that the incentive scheme proposed under DCP288 represents a practicable proposal and should facilitate effective competition between suppliers, better facilitating objective (b). Industry should consider reviewing the scheme over time, to ensure it is operating as intended and in light of any emerging issues from the GTDIS. If evidence emerged of a material cross subsidy that was harming competition and distorting the market, industry may want to consider whether there is merit in revisiting some of the distributional impacts. Industry should also consider reviewing the incentive scheme and approach to theft given the likely impact the roll-out of smart meters will have.

Decision notice

In accordance with standard licence condition 22.14 of the Electricity Distribution Licence, the Authority hereby directs that modification proposal DCP288: Introduction of the Electricity Theft Detection Incentive Scheme be made.

Rob Salter Church
Interim Executive Director, Consumers & Markets

Signed on behalf of the Authority and authorised for that purpose