

Modification proposal:	Uniform Network Code (UNC) 308: (UNC308) 'Appropriate use of the terms Surety and Security in UNC Section V'		
Decision:	The Authority ¹ directs that this proposal be made ²		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	14 January 2011	Implementation Date:	To be confirmed by the Joint Office

Background to the modification proposal

In 2005 Ofgem published its best practice guidelines for gas and electricity network operator credit cover ('the guidelines')³. The aim of the guidelines was to ensure that network operators' credit cover and payment terms were proportionate, allowing network operators to properly manage, rather than wholly avoid, any exposure to financial risk.

Review Proposal 252 was raised in April 2009. Its aim was to review the Uniform Network Code (UNC) credit arrangements for transportation charges and consider whether they remained fit for purpose in light of the many credit issues since the publication of the guidelines. Examples of such issues are the collapse of financial institutions such as Lehman Brothers and the wider 'credit crunch'. The Review Group came forward with 14 recommendations, each of which has now been raised as an individual modification proposal.

The modification proposal

It was noted by the Review Group that the terms *Surety* and *Security* are used throughout Section V, but not in a consistent fashion.

While it does not seek to add *Surety* and *Security* as defined terms within the UNC, this proposal does seek to clarify the usage of these terms within Section V, in particular being more specific about the credit tools to which those terms and the associated provisions relate.

UNC308 sets this out as follows:

Instrument of credit	Form
Letter of Credit	Surety
Guarantee	Surety
Deposit Deed	Security
Pre-payment Agreement	Security

¹ The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

³ <http://www.ofgem.gov.uk/Pages/MoreInformation.aspx?file=9791-5805.pdf&refer=Licensing/IndCodes/CreditCover>

The Proposer considers that UNC308 will further relevant objective (f)⁴ by removing any ambiguity around the application of the UNC provisions where different credit instruments are utilised.

UNC Panel³ recommendation

At its meeting of 19 August 2010 the UNC Modification Panel voted unanimously to recommend that this proposal be implemented.

The Authority's decision

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 11 January 2011. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR⁵. The Authority has concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC; and
2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties⁶.

Reasons for the Authority's decision

Of the eleven responses to the Joint Office's consultation, seven were in support of its implementation, while a further two offered qualified support and two offered comments only. We agree with respondents and the UNC Panel that UNC308, being largely a housekeeping proposal, should be assessed only against relevant objective f). UNC308 has no discernible impact upon the other relevant objectives.

Relevant Objective (f): the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;

The two respondents who offered qualified support for the proposal stated that they did not necessarily agree with the table setting out the meaning of Surety and Security, but did not disagree with the actual use of these terms in the legal text. They suggested that it would add clarity if *Surety* and *Security* were added as defined terms within the UNC, but did not offer their own definitions of these terms. While it may add clarity for *Surety* and *Security* to be defined terms within the UNC, we do not consider that they have any meaning that is particular to that document or would in any way differ from a standard dictionary definition. Although the table aided understanding of the modification proposal, giving context to the various references to *Surety* and *Security* throughout Section V, it does not feature in the actual legal text that would be modified.

In contrast, one of the respondents who provided comments only, agreed with the table which illustrated which instrument of credit is considered to be surety and which is security. However, they did raise a concern with the legal text, noting that it conflicted with the legal text for UNC300: *'Introduction of Fitch as an allowable Credit Rating*

⁴ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547

Agency for the purpose of Code Credit Arrangements'. This issue has since been addressed and the legal text submitted as part of the FMR dated 06 January 2011 includes text implemented on 16 December 2010 as a result of modification UNC300.

It appears that the terms *Surety* and *Security* have been used interchangeably within the UNC without there being any intention to draw a particular distinction between the two. However, to the extent that those terms are commonly perceived to relate to different types of credit instruments, we consider that more precise and deliberate references to those terms will aid understanding of the UNC and reduce the potential for misinterpretation. For instance, following the implementation of UNC308 it will be clearer that any additional credit cover the GT may require to be lodged in accordance with Section V 3.1.1 may be in the form of either *Security or Surety*, allowing the User to utilise the full range of credit instruments permitted under the UNC.

It is not clear within the FMR to what extent the existing provisions have in the past caused confusion, though as this modification will not impose any implementation costs we consider that even a marginal improvement in the clarity of the UNC would be of value and further facilitate relevant objective f).

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority, hereby directs that modification UNC308: '*Appropriate use of the terms Surety and Security in UNC Section V*' be made.

Rachel Fletcher

Partner, Distribution

Signed on behalf of the Authority and authorised for that purpose