Draft Modification Report
RG0252 Proposal 13a: Removal of DNOs as Users from UNC TPD V3 and V4
Modification Reference Number 0311
Version 1.0

This Draft Modification Report is made pursuant to Rule 9.1 of the Modification Rules and follows the format required under Rule 9.4.

1 The Modification Proposal

WWU raised Review Group 0252 "Review of Network Operator Credit Arrangements" in April 2009. This was convened to discuss the appropriateness of the existing credit management arrangements , taking into account the many credit related issues which had occurred since the publication of Ofgems "Best practice guidelines for gas and electricity network operator credit cover" (BPG) document.

This specific Modification Proposal (13a) is an alternative to Modification Proposal (13) raised by Scotia Gas Networks (SGN). However, it has been raised as a standalone Modification Proposal due to the restrictions on the timing of raising Alternative Modification Proposals. The Modification Proposal mirrors the intent within SGN's Modification Proposal of seeking to remove the current credit requirement within UNC (V3.3.4) which would lead to the unnecessary over securitisation of DNO's from October 2012. Removing this DNO reference would additionally remove the differential treatment which currently exists whereby NGD and NTS are a single entity for credit purposes (and as such NGD are not governed by this credit requirement but the iDNs are).

This Modification Proposal also seeks to amend other anomalies within UNC TPD Sections V3 and V4 which if amended will better facilitate the Transporters Licence conditions (against the existing UNC), than the Modification Proposal raised by SGN (proposal 13).

The table below sets out the anomalies in UNC TPD V impacted by this proposal contrasted with that raised by SGN

	Proposal 13 (SGN)	Proposal 13a (WWU)
1. Removal of 12 month iDN securitisation requirement for NTS Exit Capacity charges	YES	YES
2. Removal of circa 51 days iDN securitisation requirement for all applicable charge types	NO	YES
3. Removal of requirement for IDNs to securitise against DN Pension charges	NO	YES
4. Removal of unworkable DN Termination facility in UNC V4	NO	YES

5. Removes unintended credit consequences of Mods 116, 127, 195AV and any future DNO charges	PARTIALLY	YES
6. Removes differential treatment of DNs by NTS in V3	PARTIALLY	YES
7. Removes potential increased security cost pass through to Shippers due to UNC requirements (above)	PARTIALLY	YES

Item 1.- Removal of 12 month securitisation requirement for NTS Exit Capacity charges. – to remove iDNs from the requirements of V3.3.4 (for the avoidance of doubt Shipper Users will be subject to this clause for any capacity they have registered at an NTS Exit Point (not NTS/LDZ Offtakes).

The inclusion of this UNC requirement arose through the implementation of UNC Modification Proposal 0195AV "Introduction of Enduring NTS Exit Capacity Arrangements". Aside from the possible parallels with NTS Entry Capacity requirements, no justification for its inclusion was in this (0195AV) Modification Proposal. All Users were to be treated the same (except National Grid Distribution) for this specific clause. A series of options, including the option covered by this Proposal, were presented to the Transmission workstream on 3rd December 2009 to deal with this specific anomaly.

The effect of this is to require DNO Users to provide, (with effect from 1 October 2012), credit cover equivalent to the cost of twelve months NTS Exit (Flat) Capacity. Currently Users' Value at Risk is defined in Section V, paragraph 3.2.1 (d) (i) and (ii). In this paragraph Value at Risk is defined as the amount invoiced to the User remaining unpaid, plus the average daily charge invoiced to the User in the previous calendar month multiplied by 20. Energy Balancing charges are excluded. Therefore, the Value at Risk for a DNO User in respect of NTS Exit Capacity Charges from October 2012 should be equivalent to the cost of circa 51 days NTS Exit (Flat) Capacity charges.

The move from providing credit cover for 51 days to credit cover for 51 days + 12 months will represent a significant increase in costs for DNO Users. WWU anticipate that it will need to securitise approximately £45M of NTS Exit Capacity Charges with National Grid NTS in October 2012 should this Modification Proposal not be implemented. The justification for this is not clear as Exit Reform does not involve any great change in the circumstances under which Exit Capacity is sold by the NTS. During RG0252 discussions and during development of Modification Proposal 0261 'Annual NTS Exit (Flat) Capacity Credit Arrangements' it was confirmed by NTS that iDNs presented a low credit risk.

Similarly, in 2009 Transmission Workstreams, NTS Exit Capacity User Commitment Strawman clearly indicated that DNOs should be excluded from the scope of such proposals.

The credit cover required for Entry Capacity is already 12 months but this is understandable in view of the greater uncertainly associated with the Entry

Capacity auction regime and the need to discourage speculative bidding. However, no such considerations apply to the Exit Capacity regime, and therefore there is no need to increase the 51 days credit cover for the iDNs.

Should this 12 month securitisation clause remain in place iDNs will need to raise a UNC Modification Proposal to cover an equivalent 12 months LDZ Exit Capacity NTS (ECN) charges, the costs of which will be borne by Users and potentially consumers.

Item 2 - Removal of circa 51 days securitisation requirement for all applicable charge types.

Transporters are heavily regulated through Licence conditions to ensure their financial viability. Securitising simply to be consistent with the requirements of (Shipper) Users is neither necessary nor is it an efficient utilisation of Transporters funds and/or credit lines.

Item 3 - Removal of requirement for IDNs to securitise against DN Pension charges

Securitisation between some Transporters in respect of Transportation charges is inconsistent and therefore this requirement should be similarly removed.

Item 4 - Removal of unworkable DN Termination facility in UNC V4

The retention of DNO User in UNC section V automatically leads to DNO Users being subject to Termination criteria and procedures. These procedures are unworkable and do not (legitimately) take account of anything other than Shipper termination. It is inappropriate and misleading therefore to have the UNC reference DNO's in this regard.

Item 5 - Removes unintended consequences of Mods 0116, 0127, 0195AV and any future DNO charges

The implementation of Proposal 0195AV "Introduction of Enduring NTS Exit Capacity Arrangements" built largely on aspects of Modification Proposal 116. Sandwiched in between these proposals was Modification Proposal 0127 "Introduction of a DN Pensions Deficit Charge" which referenced DNO Users for invoicing and credit purposes. The subsequent implementation of 195AV carried the unintended consequence whereby NTS Exit charges were automatically deemed a DNO User charge requiring securitisation with National Grid NTS. This was never intended and should therefore be removed. Similarly, should any future DNO charge be introduced, it should not automatically be subject to the general User rules, unless specifically warranted.

Item 6. Removes differential treatment of DNs by NTS in V3

The iDNs (WWU, SGN and NGN) are presently required to securitise with National Grid Transmission and each GDN bears these security costs. National Grid Distribution are not required to securitise (National Grid is viewed as single entity for these purposes, albeit they have different licences). National Grid distribution does not bear any such costs.

Item 7 - Removes potential increased security cost pass through to Shippers due to UNC requirements

Any securitisation required of DNOs by National Grid NTS in respect of 51 days credit or 12 months credit will be necessarily passed through to Shippers and potentially Consumers. Current UNC wording does not allow DNs to request Shippers to secure an extra 12 months charges. Should this proposal (or proposal 13) not be implemented iDNs will raise a Modification Proposal to mirror these security arrangements and necessarily back off its risk. In view of WWU's RAV (in comparison to National Grid NTS), the maximum unsecured value for credit will be significantly lower and therefore lead to Shippers having to provide higher levels of costly security to iDNs, with no benefit being gained.

RG0252 discussions resulted in all members supporting the intent set out in Proposal 13, whereas elements of the Review Group supported the fuller intentions of Proposal 13a.

Suggested Text

V 3 and V4

V 3.1.2 In this paragraph 3 references to:

(a) Users ~~include~~ excludes DNO Users;

V 4.1.6 In this paragraph 4 references to:

(a) Users ~~include~~ excludes DNO Users;

2 User Pays

a) Classification of the Proposal as User Pays or not and justification for classification

This Proposal is not classified as a User Pays Modification Proposal as it does not create or amend any User Pays Services.

b) Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification

No User Pays charges applicable.

c) Proposed charge(s) for application of Users Pays charges to Shippers

No User Pays charges applicable to Shippers.

d) Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from xoserve

No charges applicable for inclusion in ACS.

3 Extent to which implementation of the proposed modification would better facilitate the relevant objectives

Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;

This proposal will assist the economic operation of the DN pipeline systems for the iDNs by avoiding an increase in the cost of operating the systems for which there is no offsetting benefit. The cost will vary depending on the credit rating of the iDN seeking the cover and the amount of cover required.

Standard Special Condition A11.1 (b): so far as is consistent with sub-paragraph (a), the coordinated, efficient and economic operation of

(i) the combined pipe-line system, and/ or

(ii) the pipe-line system of one or more other relevant gas transporters;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (c): so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (d): so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition:

(i) between relevant shippers;

(ii) between relevant suppliers; and/or

(iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers;

The Proposer believes that implementation would further the GT Licence 'Code relevant objective' of the securing effective competition between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers. Removing this UNC requirement would re-instate a level playing field whereby all Distribution Networks were treated the same by National Grid NTS.

Standard Special Condition A11.1 (e): so far as is consistent with sub-paragraphs (a) to (d), the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards… are satisfied as respects the availability of gas to their domestic customers;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (f): so far as is consistent with sub-paragraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;

Removing this requirement would ensure all Users had similar credit arrangements with all Distribution Networks. Retaining the existing requirement would create a two tier credit arrangement with users requiring proportionately higher levels of securitisation with every Distribution Network except National Grid Distribution.

4 The implications of implementing the Modification Proposal on security of supply, operation of the Total System and industry fragmentation

No implications on security of supply, operation of the Total System or industry fragmentation have been identified.

5 The implications for Transporters and each Transporter of implementing the Modification Proposal, including:

a) Implications for operation of the System:

There are no implications for operation of the System.

b) Development and capital cost and operating cost implications:

There are no cost implications.

c) Extent to which it is appropriate to recover the costs, and proposal for the most appropriate way to recover the costs:

No additional cost recovery period is proposed.

d) Analysis of the consequences (if any) this proposal would have on price regulation:

Not applicable.

6 The consequence of implementing the Modification Proposal on the level of contractual risk of each Transporter under the Code as modified by the Modification Proposal

The contractual risk to National Grid NTS (from the non NG Distribution Networks) theoretically increases, however Transporters broader Licence obligations in terms of indebtedness and required investment grade requirement etc more than compensate for this.

7 The high level indication of the areas of the UK Link System likely to be affected, together with the development implications and other implications for the UK Link Systems and related computer systems of each Transporter and Users

No changes have been identified.

8 The implications of implementing the Modification Proposal for Users, including administrative and operational costs and level of contractual risk

Administrative and operational implications (including impact upon manual processes and procedures)

No implications have been identified.

Development and capital cost and operating cost implications

To be advised by Users.

Consequence for the level of contractual risk of Users

No consequences have been identified.

9 The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non Code Party

The only theoretical (increased level of) risk rests with National Grid NTS with the proposal.

10 Consequences on the legislative and regulatory obligations and contractual relationships of each Transporter and each User and Non Code Party of implementing the Modification Proposal

No consequences have been identified.

11 Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantages

- ensures DNOs are not over securitised in respect of potential charges to National Grid NTS.
- removes differential treatment between NG Distribution and other DNO's in respect of credit arrangements with NG NTS.
- Removal of over securitsation will reduce costs for shippers (and consumers)
- Removes the need to raise a subsequent UNC proposal seeking to ensure Shippers securitise 12 months worth of LDZ ECN Charges with some DNOs.
- Removes unintended consequences of Modification Proposal Proposal 0195AV
- Makes UNC Termination arrangements not applicable to Transporters.

Disadvantages

- Decreases securitisation for National Grid NTS in respect of NTS capacity charges booked by some GDNs

12 Summary of representations received (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)

Written Representations are now sought in respect of this Draft Report. Consultation End Date: ***30 July 2010***

13 The extent to which the implementation is required to enable each Transporter to facilitate compliance with safety or other legislation

Implementation is not required to enable each Transporter to facilitate compliance with safety or other legislation.

14 The extent to which the implementation is required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence

Implementation is not required having regard to any proposed change in the methodology established under paragraph 5 of Condition A4 or the statement furnished by each Transporter under paragraph 1 of Condition 4 of the Transporter's Licence.

15 Programme for works required as a consequence of implementing the Modification Proposal

No programme of works would be required as a consequence of implementing the Modification Proposal.

16 Proposed implementation timetable (including timetable for any necessary information systems changes and detailing any potentially retrospective impacts)

It is suggested that this Proposal be implemented on 1st October 2010 to coincide with the implementation of the other credit proposals being considered in this timeframe. Should this date not be achievable, then implementation could take place immediately following an Authority direction

17 Implications of implementing this Modification Proposal upon existing Code Standards of Service

No implications of implementing this Modification Proposal upon existing Code Standards of Service have been identified.

18 Recommendation regarding implementation of this Modification Proposal and the number of votes of the Modification Panel

19 Transporter's Proposal

This Modification Report contains the Transporter's proposal to modify the Code and the Transporter now seeks direction from the Gas and Electricity

Markets Authority in accordance with this report.

20 Text

Representations are now sought in respect of this Draft Report and prior to the Transporters finalising the Report.

For and on behalf of the Relevant Gas Transporters:

Tim Davis
Chief Executive, Joint Office of Gas Transporters