

Credit Risk Management Transportation – Rules & Procedures

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Document Control

Version	Date	Reason for Change
2.0	1 May 2006	Format revisions: Title page, Document Control, Development of Rules, Contents page, headers and footers. Alignment with Version 2.02 of UNC. Replacement of Blackwater 2 Ltd. with Wales & West Utilities (WWU)
3.0	17 August 2006	Update WWU office address.
4.0	1 May 2007	Include implementation of UNC credit modifications 0107 & 0113. Remove WWU Portfolio criteria. Allow for Transportation Charging changes.

Development of Code Credit Rules

1. The requirement to publish the Code Credit Rules is specified in Section V 3.1.2 & 3.1.3 of the Transportation Principal Document of the Uniform Network Code (UNC). This section also provides for the document to be revised from time to time. The provision reads¹:

The '**Code Credit Rules**' are the rules from time to time established and revised by the Transporter and issued to Users setting out (inter alia):

- (a) the principles on which the Transporter will assess and establish Code Credit Limits;
- (b) the basis on which a User may (with a view to increasing its Code Credit Limit) provide surety or security for Relevant Code Indebtedness, or (with a view to reducing its Relevant Code Indebtedness) make prepayments to the Transporter;
- (c) procedures by which a User may discuss its Code Credit Limit with the Transporter.

The Code Credit Rules do not form a part of the Code and (but without prejudice to the further provisions of this paragraph or to anything done pursuant to the Code Credit Rules) nothing in the Code shall make compliance with such rules an obligation of the Transporter or Users.

2. The Code Credit Rules set out below meet Wales & West Utilities Ltd's (WWU's) obligation to prepare rules, while the Document Control Section records changes that have been made to the rules. The document is published on the Joint Office of Gas Transporters' website, www.gasgovernance.com and on the WWU website: www.wwutilities.co.uk.
3. The UNC does not provide for Users to be consulted when changes to these rules are proposed. However, WWU would welcome comments from Users on the published rules at any time, which should be sent to sue.davies@wwutilities.co.uk. When WWU wishes to revise the Code Credit Rules, we intend adding the proposed revision to the agenda of the UNC Committee such that the views of User representatives can be sought prior to any revisions being made.

¹ Correct as at 01 May 2007, Version 2.38 of the UNC.
Code Credit Rules

Introduction

This Document has been designed to provide existing and prospective Users with all the information they need about the Code Credit Rules and how they are applied by Wales & West Utilities Ltd. (WWU) in managing its transportation credit risk exposure to Users.

The Document sets out to answer those questions which are most commonly asked by Users, and gives an overview of how credit limits are established, secured and monitored. For ease of reference we have also provided cross references to Uniform Network Code (UNC), to provide you with a fuller explanation of a particular legal or technical issue. We will endeavour to update this document following any relevant UNC modifications.

Once you have read the Document, WWU will be pleased to discuss your requirements further and to answer any questions which you may have. Contact details can be found at the back of the Document.

It should be noted that the Code Credit Rules apply to transportation services only and that a further credit limit will be required in respect of Energy Balancing charges. Further information can again be found at the back of the Document.

The Code Credit Rules

What are the Code Credit Rules?

Under the UNC, all Users must obtain a Code Credit Limit from WWU prior to the commencement of trading. The Code Credit Rules describe how that limit is determined, the security that WWU may require from a shipper to support its Code Credit Limit and the process WWU will use to monitor utilisation against that limit.

The Code Credit Rules are the processes and procedures described in this Document and provide the framework by which WWU can ensure that it manages its credit risk exposure consistently across all shippers.

Who should I talk to about the Code Credit Rules?

Responsibility for setting credit limits for Users and for monitoring exposure rests with the Transporter's Credit and Risk Management Team who can be contacted at the address at the back of the Document.

Code Credit Limits

What does the Code Credit Limit represent?

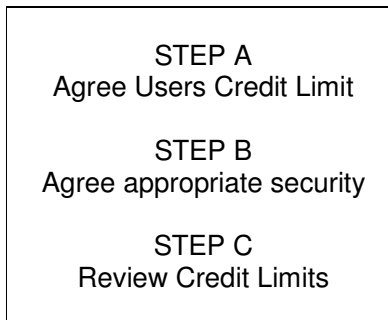
The Code Credit Limit represents the maximum indebtedness that WWU will extend to a User. Indebtedness arises as a result of transportation services provided to the User and includes amounts both invoiced and those services which have been provided but not yet invoiced. Indebtedness therefore changes on a daily basis as further charges are accrued.

Credit Limit Determination

The process that derives a counterparty credit limit is set out below. WWU will, subject to commercial prudence, endeavour to allocate Users with a credit limit that will not inhibit their trading activities.

The credit limit determination process has three component steps outlined in Figure 1 below.

Figure 1



Step A - What level of Credit will I need?

First of all it is necessary to estimate the User's peak trading requirement (or estimated peak indebtedness). WWU will use a number of different modelling techniques to arrive at this estimate.

For a new User, various parameters are taken into account, for example the predicted level and type of business activity, and the predicted size and type of sites that may form part of its customer portfolio. WWU uses all this information to predict the scale of charges (including VAT) for 63 day's peak trading. This amount is then used as a basis for the calculation of a Code Credit Limit.

For an existing User, the last twelve months' invoiced charges will be reviewed to assess peak historical exposure and adjusted for any anticipated changes to WWU Transportation Charging or the User's portfolio of supply points.

Following application of these processes and consultation with the User to arrive at a peak trading requirement, this figure must be divided by 85% to arrive at the Code Credit Limit.

Step B - On what basis is this Limit provided?

A User may select, from three possible options, the basis upon which the credit limit will be provided.

1. Unsecured Credit Limit

An unsecured credit limit may be based upon either the credit rating of the User, User payment history or an Independent Assessment. The rating used by WWU will be the lowest rating provided by the approved rating agencies.

The current transporter approved rating agencies are Moody's and Standard & Poors; however it should be noted that WWU shall be entitled to amend the list of approved rating agencies at its discretion.

2. Secured Credit Limit

The credit limit is set by reference to the security provided by the User.

3. Prepayment

Payment is one calendar month's estimated charges made in advance by the User. Details of the estimated charges are provided to the User by the 20th of the preceding month. Payment is then due by the last working day of the month. In recognition of the cash flow disadvantage this provides to the User, WWU may pay a use of funds amount which will be calculated using a rate referenced to three months sterling LIBID.

A prepayment proforma agreement as defined by WWU must be signed if this security method is to be used.

What Security Options are acceptable to WWU?

The format and wording of the security must be acceptable to WWU; there are a number of these. However, the usual options are a guarantee from the shipper's parent company (which is acceptable provided that the guarantor has an investment grade rating) or a guarantee issued by an acceptable financial institution, often called an irrevocable standby Letter of Credit, which must be presentable at a financial institution office located in the United Kingdom.

Note: The Guarantee or irrevocable standby Letter of Credit will have a deemed value of zero for the purposes of security, 30 days prior to maturity.

Pro-forma copies of WWU's standard Security Documentation are available on request.

WWU will also consider any combination of the options which matches the User's overall requirements.

Restrictions on Credit Exposure

The restrictions on credit exposure are defined in the UNC Transportation Principal Document (TPD). The specific clauses are listed below:

Section V 3.1.1:

"... The Transporter will determine and assign to each User a Code Credit Limit, which may comprise of an Unsecured Credit Limit calculated in accordance with

paragraph 3.1.6 and/or security or surety provided in accordance with paragraph 3.4. The Transporter shall keep each User informed of its Code Credit Limit (as revised in accordance with the Code) for the time being. The Transporter shall limit the Unsecured Credit Limit to any User and related company to a maximum of two percent (2%) of the Regulatory Asset Value (The 'Maximum Unsecured Credit Limit')..."

The maximum Unsecured Credit Limit would only be made available to companies obtaining the highest credit rating i.e. AAA rated by either Moody's or Standard & Poor's Investor Rating Services.

Section V 3.1.6:

Where a User has an Approved Credit Rating, such User's Unsecured Credit Limit at any time shall be calculated as that percentage (%) of the Maximum Unsecured Credit Limit by reference to the User's Approved Credit Rating as follows:

Approved Credit Rating		User's % of Maximum Unsecured Credit Limit
Standard & Poor's	Moody's Investor Service	
AAA/AA	Aaa/Aa	100
A	A	40
BBB+	Baa1	20
BBB	Baa2	19
BBB-	Baa3	18
BB+	Ba1	17
BB	Ba2	16
BB-	Ba3	15

Section V 3.1.7:

Subject to paragraph 3.1.10, where a User does not have an Approved Credit Rating, or a User's Approved Credit Rating is less than Ba3 awarded by Moody's Investment Services or an equivalent rating by Standard and Poor's Corporation, such User may obtain an Unsecured Credit Limit by:

- (a) payment history in accordance with paragraph 3.1.8 below; or
- (b) independent assessment in accordance with paragraph 3.1.9 below

provided that a User shall only be able to obtain an Unsecured Credit Limit by one of the above methods at any one time.

Section V 3.1.8:

The Transporter may allocate an Unsecured Credit Limit to a User based upon the period of time elapsed that such User has paid all invoices by their due date for payment in accordance with Section S, such that after a calendar month, a User may be allocated an Unsecured Credit Limit on the basis of 0.4% of the relevant Transporter's Maximum Unsecured Credit Limit over a 12 Month period and increasing on an evenly graduated basis each Month up to a maximum of 2% of the relevant Transporter's Maximum Credit Limit after 5 Years.

Section V 3.1.9:

Where a User has been allocated an Unsecured Credit Limit pursuant to 3.1.8 above, and such User subsequently fails to make payment of any invoice issued in accordance with Section S, then its Unsecured Credit Limit shall be deemed to be valued at zero from the date of such payment default.

Section V 3.1.10:

Upon request from a User, the Transporter may appoint one of a panel of 3 independent agencies to allocate an Unsecured Credit Limit to the User where:

- (a) such User is unable to obtain an Approved Credit Rating (up to a maximum of 20% of the relevant Transporter's Maximum Unsecured Credit Limit); or
- (b) such User has an Approved Credit Rating below Ba3 (awarded by Moody's Investment Services or an equivalent rating by Standard and Poor's Corporation) (up to a maximum of 13.33% of the relevant Transporter's Maximum Unsecured Credit Limit),

a score of between 0 and 10 will be allocated to the User in accordance with the following table to calculate the User's Unsecured Credit Limit:

Independent Assessment Score	% of Transporters Maximum Unsecured Credit Limit
10	20
9	19
8	18
7	17
6	16
5	15
4	13 ^{1/3}
3	10
2	6 ^{2/3}
1	3 ^{1/3}
0	0

Step C - How often are Credit Limits reviewed?

WWU will review a User's credit limit at least every 12 months. This review will commence 3 months prior to the expiry of any security documents held by WWU. However, WWU may initiate a review at any other time if there have been changes to a User's circumstances, and may seek authorisation to request appropriate bank and trade references.

Section V 3.2.4 of the UNC TPD covers review of credit limits as follows:

A User's Code Credit Limit may from time to time be reviewed and revised, in accordance with the Code Credit Rules, save where either paragraph 3.2.5 or 3.2.6 applies, in the case of (a), (b), (d) and (e) on notice of not less than 30 days, or in the

case of (c) below on notice of not less than 2 Business Days following the Business Day on which a notice is issued in accordance with 3.2.9, (or in any such case, such lesser period agreed by the User) to the User;

- (a) at intervals of approximately 12 months;
- (b) at the User's request (but subject to paragraph 3.2);
- (c) where any published or Specially Commissioned Rating of the User or any person providing surety for the User is revised downwards;
- (d) where (but without prejudice to any requirements of the Code Credit Rules) any instrument of surety or security expires or is determined;
- (e) at the Transporter's request where the Transporter has reasonable grounds to believe that the effect of the review will be to reduce the Users Code Credit Limit.

A User may also request a change to its credit limit or form of security at any time subject to 10 days written notice.

Section V 3.4.3:

Following a request by a User under paragraph 3.4.2, the Transporter will as soon as reasonably practicable and, except where the User also requests a review (by an agency appointed by the Transporter for such purposes) and revision of its Code Credit Limit, in any event not more than 10 Business Days after such request, release security, or agree to a reduction in surety, to such extent or by such amount as will permit the condition in paragraph 3.4.4 to be satisfied.

Provision of alternative security may be necessary to accommodate the request.

Section V 3.4.4:

The condition referred to in paragraph 3.4.3 is that the amount of the User's Relevant Code Indebtedness at the date of such release or reduction is not more than 85% of the amount of the Users Code Credit Limit, determined in accordance with the Code Credit Rules on the basis of the release of security or reduction in surety (and taking into account any alternative surety or security provided by the User).

Should a User cease trading in respect of Transportation services, a minimal level security will be required for a period of 18 months from the last issued invoice payment due date to cover potential invoice adjustments. The minimal level of security will be discussed and agreed with the User.

Credit Limit Utilisation

How is Credit Limit Utilisation measured?

At any point in time, a User's indebtedness will be measured under the three headings below. The amounts are for illustrative purposes only, and in practice will vary between Users and will change each day:

Invoiced & due	£ 500,000
Invoiced and not yet due	£ 1,500,000
Services provided not yet invoiced	£ 275,000
Total indebtedness	£ 2,275,000

Credit limit utilisation is the total indebtedness, less any pre-payments, expressed as a percentage of the User's credit limit.

Indebtedness is described in Section V 3.2.1b of the UNC TPD as:

- (i) the aggregate amount, other than in respect of Energy Balancing Charges, for which a User is at any time liable to the Transporter pursuant to the Code or any Ancillary Agreement, determined on the basis of amounts accrued (and in accordance with paragraph (c) where applicable) and irrespective of whether such amounts have been invoiced under Section S or (where invoiced) have become due for payment less
- (ii) any amount which has been paid to the Transporter by the User by way of prepayment on the basis that the Transporter may apply such amount without the Users consent in or towards payment of amounts referred to in paragraph (i), and which has not yet been so applied.

What about Invoice Queries?

If a User has submitted invoice queries in line with the process laid down in the UNC, the value of the valid withholds will be given due consideration when reviewing a User's indebtedness.

Section V 3.2.2 & V 3.2.3 of the UNC TPD defines how invoice queries are treated when calculating indebtedness as follows:

For the avoidance of doubt, the amount of a User's Relevant Code Indebtedness shall be determined by reference to the relevant provisions of the Code, and nothing in the Code shall be construed as withdrawing from a User any right to dispute whether the Transporter has correctly calculated such amount in any case, or from the Transporter any right to dispute the validity of any Invoice Query submitted by any User.

Without prejudice to paragraph 3.2.2, where a User has submitted an Invoice Query in accordance with Section S 4.2.1 in respect of any Invoice Document, the Transporter will review and give due consideration to such Invoice Query.

How will the User be notified of its Credit Limit Utilisation?

Each User will be required to nominate two contacts to whom notification of its credit limit utilisation can be sent.

Formal notification will be sent when utilisation rises above 70% of the Code Credit Limit. This will act as a warning that exposure, although manageable, can quickly rise from this level up to the credit limit.

The User will receive another formal notification when utilisation reaches 85% of the Code Credit Limit.

During this formal notification process the Credit and Risk Management team will discuss with the User ways to rectify the situation e.g. WWU may ask for a payment on account to ensure that indebtedness remains within the agreed limit or undertake a review of the Code Credit Limit.

If utilisation remains above 85%, WWU may apply sanctions, as detailed in the UNC until such time as utilisation reduces to below 85% of the Code Credit Limit. It is for this reason that WWU divides the anticipated peak trading requirement by 85% to arrive at the Code Credit Limit.

Section V 3.3.2 of the UNC Principal Document describes the sanctions that may be applied by WWU:

Where and for so long as the Relevant Code Indebtedness of a Shipper User for the time being exceeds 85% of the User's Code Credit Limit, the Transporter shall be entitled to reject or refuse to accept all or any of the following by the relevant User:

- (a) an application for System Capacity or increased System Capacity at any System Point under Section B or G5;
- (b) in relation to the NTS, a System Capacity Trade under Section B5 in respect of which the User is Transferee User;
- (c) a Supply Point Nomination or Supply Point Confirmation under Section G, other than a Supply Point Renomination or Supply Point Reconfirmation (unless made in the context of an application under paragraph (a))

until such time as the User's Relevant Code Indebtedness is reduced to less than 85% of its Code Credit Limit.

What happens if a User exceeds its Credit Limit?

In view of the notifications WWU sends to User at 70% and 85% utilisation of the Code Credit Limit, we would hope to avoid situations where a User's Code Credit Limit is exceeded by understanding the User's future requirements and agreeing an increased limit in accordance with the Code Credit Rules.

Should a User's utilisation exceed 100% of its Code Credit Limit, and WWU and the User are unable to agree an increase in the credit limit and ongoing dialogue between the parties has not led to reduced indebtedness in accordance with the Code Credit Limit, then WWU may

call upon any security or surety that has been provided by the User. Alternatively WWU may terminate a User's UNC Contract in accordance with UNC TPD Section V 3.3.3.

Section V 3.3.3 of the UNC TPD describes the sanctions that may be applied by WWU if a User's utilisation level exceeds 100% of its Code Credit Limit:

Section V 3.3.3:

Subject to paragraph 3.3.1, where and for so long as the Relevant Code Indebtedness of a User for the time being exceeds 100% of the User's Code Credit Limit, the Transporter may give Termination Notice (in accordance with paragraph 4.3) to the User.

The formal exposure milestones will be as follows:

- The User will receive formal notification from WWU when measured limit utilisation rises above 70%. This will act as a warning that exposure, although manageable, can quickly rise from this level to the approved limit in the event of any difficulties being encountered.
- The User will receive another formal notification when the User's measured utilisation reaches 85%. Furthermore, at this point WWU reserves the right to apply sanctions, as detailed in the UNC.
- Throughout the escalation process, WWU will maintain contact with the User to understand the reason for increases in credit exposure levels and will provide support and assistance where possible.

Default can occur in a number of situations, one of which is when the User is in breach of its credit limit. A User may be given a short period of time in which to rectify any breach, alternatively the User and WWU may agree an action plan to rectify the position.

Termination will deal with the processes of 'termination of supply' and recoveries of debt owed to WWU. The User will be formally notified of the date set by WWU to terminate its shipper Agreement.

Following termination, the provisions of the Gas Act, WWU's GT licence, and the Shipper & Supplier Licences will operate.

What happens if a User does not pay Transportation invoices on their payment due date?

Section S 3.5.1 & S 3.5.2 of the UNC TPD state:

Without prejudice to Section V4.3.1, where any amount payable under an Invoice is not paid on or before the Invoice Due date, the paying party shall pay interest, after as well as before judgement, at the Applicable Interest Rate, on the unpaid amount from the Invoice Due Date until the Day on which payment is made.

For the avoidance of doubt paragraph 3.5.1 shall not be construed as permitting late payment of any Invoice Amount.

Further Information

If, having read the Document, you still have unanswered questions or would like further clarification, then please do not hesitate to either write to or telephone the Credit and Risk Management Team at the following address:

Credit and Risk Management
Wales & West Utilities Ltd
Wales & West House
Spooners Close
Coedkernew
Newport
NP10 8FZ
Telephone: 029 20278839
Facsimile: 0845 0720855

Energy Balancing

All Users require a separate Secured Credit Limit in respect of all Energy Balancing charges.

The management of the community credit risk exposure associated with Energy Balancing activity is governed by criteria set out in the UNC TPD Section X ('Energy Balancing Credit Management'). In addition, a separate document called the Energy Balancing Credit Rules explains the practical operation of the principles established in the supplement. A team within xoserve called Credit and Risk Management - Energy, carries out this process. UNC Users requiring more information should contact:

Credit and Risk Management – Energy
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Solihull
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