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30 July 2010

Dear Bob,

**Re: UNC Modification Proposals 0298 to 0311 – Credit Modifications**

Thank you for the opportunity to provide representations of the above noted Modification Proposals. Northern Gas Networks (NGN) is supportive of all 14 of the modifications that have been raised as a consequence of Review Group 0252. NGN was an active participant in Review Group 0252 and agrees that all of the associated credit Modification Proposals reflect the conclusions of this Review Group.

Please find below NGNs comments in respect of each of the Modification Proposals.

**Modification Proposal 0298**

This Proposal is supported by NGN as it proposes to bring more clarity by removing anomalies to UNC TPD Section V and providing clarity on the application of UNC Section V3. More specifically the proposal seeks to exchange the 20% minimum increase currently linked to a change in Transportation Charges, which Users have a minimum of two months notice of, to a test on materiality based on unexpected or step changes in a Users Portfolio, such as would be expected to result in a Supplier of Last Resort appointment or acquisition of another Users portfolio. NGN believes it is more appropriate to provide additional time for provision of additional security in this case as the event is more likely to take place with short notice.

The Proposal also seeks to remove the term Bi-lateral Insurance from UNC Section V3.4.5 and V3.4.6. NGN supports the removal of this as we have not been able to identify a product to meet the criteria defined within UNC, and removal of this would therefore avoid any confusion in the future to both Transporters and Users should a User elect to utilise this form of security.

The removal of 80% value of Surety and Security clause in UNC V3.3.2 (a) is supported by NGN as during the Review Group 0252 discussions there was doubt raised that it may not be enforceable to downgrade the face value of lodged security.

#### Modification Proposal 0299

This Proposal seeks to align the timelines in UNC Section S and V in which Transporters may apply portfolio sanctions to Users. NGN supports this proposal as it would bring more clarity and consistency to the UNC as to which date Transporters may use when beginning the process of applying portfolio sanctions. The shorter date could prevent the User from increasing their level of indebtedness as a result of increasing their portfolio, thereby reducing the credit risk to Transporters and also to the industry.

#### Modification Proposal 0300

NGN supports this Proposal which introduces Fitch Rating as an acceptable Credit Rating Agency (CRA) in addition to Standard and Poor's and Moodys Investment Services in order to obtain an unsecured credit limit based on the Investment Grade Rating of the User. The implementation of this Modification Proposal will offer greater choice when selecting a CRA and reduce potential barriers to entry by not restricting the agencies.

The Proposal seeks to achieve this by introducing a new defined term instead of referring to the agencies by name each time. This will reduce administration for future changes, and will reduce the risk of references being missed.

#### Modification Proposal 0301

This Proposal seeks to remove Specially Commissioned Ratings as an acceptable tool for obtaining an Unsecured Credit Limit and is supported by NGN. This method of credit rating provides a snapshot rating, which is only valid at the time of assessment. It cannot be continuously monitored by the rating agency or the Transporter in the same way as published or public ratings, which therefore gives rise to inconsistencies between the methods of obtaining an Unsecured Credit Limit based on the Investment Grade Rating of the security provider. This also poses a risk to Transporters and other Users if the risk profile was to dramatically change.

Specially Commissioned Ratings are also expensive to obtain, and it is NGNs belief that this could be the reason that this credit tool has not been utilised by any User and removal is therefore an appropriate action.

#### Modification Proposal 0302

Currently UNC permits Users to obtain an Unsecured Credit Limit which is capped based on the relevant Transporter's published Regulatory Asset Value (RAV). This Modification Proposal seeks to add clarity by specifying that the RAV used will be the RAV published by the Authority in its relevant Price Control Final Proposal updated for current prices.

This Proposal is supported by NGN as it gives clarity as to which RAV figure is to be used when setting Unsecured Credit Limits. This will also provide consistency between the RAV used by each relevant Transporter.

#### Modification Proposal 0303

This Proposal seeks to oblige Users to maintain a Code Credit Limit at a reasonable and appropriate level by obliging those who receive 100% VAR notices in two consecutive calendar months to establish a CCL to the value of the value of the highest 100% VAR notice in the preceding two month period.

NGN support this Proposal as Users will be required to provide and maintain appropriate credit cover for their portfolio size. This will result in reduced the risk to Transporters and ultimately Users in the event that bad debt costs may be passed on.

#### Modification Proposal 0304

NGN has raised and is supportive of this Proposal which aims to introduce greater clarity on the scoring mechanism currently within UNC Section V3.1.7 and to prevent Transporters from using different methodologies for establishing the Maximum Unsecured Credit Limit based on the Independent Assessment Score.

The modification seeks to implement a table similar to that used by the Distribution Connection and Use of System Agreement (DCUSA) into the UNC to add clarity on the application of the Independent Assessment Scores. The UNC currently offers Users a choice from a panel of three agencies for each Transporter. In order to simplify this and avoid divergence between the Transporters NGN believes that the specification of three widely used and acceptable credit rating agencies is the best method of achieving this.

#### Modification Proposal 0305

Modification Proposal 0305 seeks to amend the payment history credit arrangements contained within Section V3.1.5 and V3.1.6 to be aligned with the recommendations of Review Group 0252. It proposes that payment history is only available to new entrants and up to the two year anniversary date of the User acceding to the UNC and further seeks to introduce a soft landing approach to missed payments resulting from administration errors. NGN understands that this process is broadly in line with the processes in the electricity regime contained with Connection and Use of System Code (CUSC).

As a result of this NGN support this Proposal as we believe that good payment history with the Transporter does not necessarily mean that a User is credit worthy as they may not be paying other creditors. The introduction of the soft landing will also reduce unnecessary administration and potentially harsh penalties where a genuine error has occurred.

#### Modification Proposal 0306

This Proposal seeks to introduce an obligation on Users to provide and maintain up to date credit security contact details to Transporters. NGN supports this Modification Proposal as there is currently no obligation for credit contacts to be kept up to date which can lead to difficulty in issuing UNC Notifications in relation to credit and settlement matters. NGN agrees that by

utilising the Transporter Agency to co-ordinate this implementation would bring further efficiencies to both Transporter and User processes.

#### Modification Proposal 0307

NGN offers support for this Proposal which seeks to reduce the level of debt at which a User could be considered to Default to that aligned with the Insolvency Act (1986). This provides consistency with commercial practice and by aligning with the Insolvency Act (1986) the value will become flexible in the event of future change to the legislation. While this reduction is significant in its absolute value, NGN is cognisant that the levels currently within UNC increased five fold at the point of Network sale in 2005 which significantly increased overall risk within the industry.

#### Modification Proposal 0308

NGN agreed that this Proposal brings consistency and greater clarity to section V3 of the UNC by correcting the terminology used within it. This should reduce any possibility of misinterpretations and ambiguity with regards to the legal text used to define terms.

NGN therefore support this proposal.

#### Modification Proposal 0309

This Proposal is supported by NGN as it provides clarity on the timeframes associated with the expiry of the different types of security cover, and therefore providing clear notification on the point at which Transporters would expect confirmation of renewal or replacement of security. This will reduce the Transporters risk of exposure during a period where there is not deemed to be any valid cover due to an imminent expiration date.

#### Modification Proposal 0310

NGN supports this Proposal which seeks to remove DNOs as Users from UNC Section V3.3.4, where currently the iDNOs and National Grid Distribution are treated differently due to the nature of the requirements. The current arrangements could result in additional cost to the iDNOs which will be passed on to Users as a result of lodging security for the purposes of NTS Exit Capacity. The removal of DNOs from this requirement is appropriate given the stringent financing requirements that DNOs need to maintain through their GT Licence.

It is NGNs belief that this requirement is an unintended consequence of the sequence of UNC Modification Proposals that ultimately implemented Exit Reform and that no justification has been identified in terms of risk for including DNOs in the requirement for credit cover for NTS Exit Capacity purposes.

Modification Proposal 0311

This Proposal builds on the principles contained within Proposal 0310 and all comments for the above proposal are also applicable to this Proposal. In addition to the removal of DNOs as Users specifically from UNC Section V3.3.4, this Proposal seeks to remove DNOs as Users from the entirety of UNC Section V3 and Section V4. This removes all security provisions requirements for DNOs in respect of applicable charge types, which includes payments for DN Pension Deficit Charges and any future charges which may become applicable.

Excluding DNOs as Users from UNC Section V4 will remove the unworkable case of Termination of a DNO from UNC, and therefore this Proposal is supported by NGN and would be the preferred solution between Proposals 0310 and 0311.

For the avoidance of doubt, NGN supports all of the above Modification Proposals and, on direction to implement from the Authority would be able to do so with immediate effect. I hope that these comments are of use and please do not hesitate to contact me should you require any further information relating to this.

Yours sincerely,



Joanna Ferguson  
Network Code Manager