

Modification Report
Notice Period for Code Credit Limit Revision (as a consequence of Credit Rating downgrade) and remedies for non-compliance with a request for provision of additional security.
Modification Reference Number 0077
Version 2.0

This Modification Report is made pursuant to Rule 8.9 of the Modification Rules and follows the format required under Rule 9.6.

1. The Modification Proposal

This Proposal seeks to implement recommendations identified within Ofgem's conclusions document "*Best Practice Guidelines for Gas and Electricity Network Operator Credit Cover*" 58/05. This document detailed the high-level principles that should be applied in respect of credit cover arrangements.

This Proposal seeks to implement elements of recommendations detailed within paragraphs 3.11 and 3.50 to 3.54 of the conclusions document.

Notice Period for Code Credit Limit Revision (as a consequence of Credit Rating downgrade)

Uniform Network Code (UNC) Section S3.1 details the invoice payment terms to which Users are obliged to adhere. UNC Section V3.2.4(c) makes provision for Transporters to review (in accordance with the Code Credit Rules) a User's Code Credit Limit as a consequence of a User's (or User's security provider) published credit rating being downgraded.

Currently, reduction of a User's Code Credit Limit in these circumstances can only take effect after a notice period of thirty-days (or a lesser period agreed by the User).

In line with the conclusions document, it is proposed that this notice period is two business days (the notice from the Transporter having been issued to the User the business day following the downgrade of the User's (or User's security provider) Credit Rating). Therefore the revised Code Credit Limit becomes effective from the third business day following the downgrade of the relevant User's credit rating.

Remedies for non-compliance with a request for provision of additional security

Where the above reassessment of a User's Code Credit Limit subsequently requires the posting of additional security, it is proposed that this request is incorporated into the above notice issued by the Transporter to the User and therefore the deadline for provision of additional security is two Business Days following issue.

It is proposed that where a User fails to provide the additional security (to return the User to a maximum 100% Code Credit Limit utilisation), with effect from the day following expiry of the notice period, a daily charge equivalent to that percentage interest rate as is set out from time to time in the Late Payments of Commercial Debts (Interest) Act 1998 be charged in respect of the credit 'shortfall'. This rate is

calculated by adding the appropriate equivalent percentage interest rate, on 30 June and 31 December each year. This rate is applicable for the following six-month periods i.e. 1 July to 31 December and 1 January to 30 June respectively. National Grid believes that this would act as an incentive to ensure appropriate credit arrangements are in place.

Additionally, it is proposed that where a User fails to provide the additional security by the required deadline, an administration fee may be levied according to the size of the credit shortfall, the fee being as follows.

Amount of credit shortfall	Value of Compensation that can be claimed
Up to £999.99	£40
£1,000 to £9,999.99	£70
£10,000 or more	£100

Overall, it is proposed that the above defined measures be applied according to the following timetable:

Relevant Day	Action
Day -3	User's (or User's security provider) Credit Rating downgraded. Transporter notified by relevant approved credit rating agency.
Day -2	Transporter issues notice to User of new Code Credit Limit (effective from day 0). If relevant, notice also issued of requirement for User to provide additional security (required by day 0).
Day 0	Effective date for new Code Credit Limit and deadline for provision of additional security (if required).
Day +1	Where additional security not provided: Interest and administration fee trigger. Transporter to issue a formal notice of credit shortfall and how position is to be remedied
Day +3	Where additional security not provided: Formal User response is required

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

National Grid believes that implementation of consistent credit processes which move towards recognised best practice would help ensure that there was no inappropriate discrimination, and no inappropriate barrier to entry, thereby facilitating the securing of effective competition between Relevant Shippers.

Corona, EDF, SGN and SSE also agreed that implementation would better facilitate the securing of efficient competition.

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

The implementation of this proposal should not have any effect on security of supply, operation of the Total System or industry fragmentation.

4. The implications for Transporters and each Transporter of implementing the Modification Proposal, including

a) implications for operation of the System:

No implications for operation of the system have been identified.

b) development and capital cost and operating cost implications:

No quantified estimates of Transporters development, capital or operating costs have been provided.

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

No cost recovery mechanism is proposed.

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

No such consequences on price regulation have been identified.

5. 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

Implementation would be expected to mitigate Transporters' risk from User default.

6. 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 systems impacts are anticipated by either Transporters or Users.

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

The Proposal may increase costs for some Users. The consequences may be particularly severe for Users that are dependent for credit support on a third party which is downgraded.

Implementation may increase the probability and size of pass through of costs by Transporters to Users in the event of default.

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

No such implications have been identified.

9. 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 such consequences are anticipated.

10. Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantages

- Increased alignment of the UNC with best practice as identified in Ofgem's conclusions document.
- Ensures credit cover continues to be sought on a non-discriminatory basis
- Significant reduction in time available to take required steps following reduction of a User's Credit Limit (reduced Transporter risk).

SGN and SSE agreed that the proposal is consistent with Ofgem's best practice guidelines

Disadvantages

- Significant reduction in time available to take required steps following reduction of a User's Credit Limit (increased Shipper risk).
- Potentially increases some Users' costs through application of penal interest rate.
- Users dependent on third parties for credit support may have insufficient time to make alternative arrangements

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

<u>Organisation</u>	<u>Abbreviation</u>	<u>Position</u>
Corona Energy	Corona	For
EDF Energy	EDF	For
National Grid UKD	NG UKD	For
National Grid NTS	NG NTS	For
RWE Npower	RWE	Against
Scotia Gas Networks	SGN	For
Scottish and Southern Energy	SSE	For
Total Gas & Power	TGP	For

RWE expressed a particular concern about the impact upon a User who relies upon a third party to provide security.

TGP in support concurred that *"setting a limit of two whole business days to provide additional cover ensures sufficient protection to the industry whilst minimising the potential of bad debt"* adding that the *"8% shortfall charge is an appropriate incentive to ensure that Users provide the extra credit prior to the deadline"*

TGP also expressed concern that the *"table indicating the timescales for actions to be taken when a party is defaulting on payment has not been included within the legal text. This is something we commented on in our response to Modification 0025, but still has not been addressed in this modification."*

The SME would respond that he believes that the legal text as drafted adequately covers the nature of the proposal. This view is also held by the relevant legal resource that provided the draft text.

12. 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.

13. 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.

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

Changes would be required in respect of operational processes and procedures were this Modification Proposal to be implemented.

15. Proposed implementation timetable (including timetable for any necessary information systems changes)

Changes would be required in respect of operational processes and procedures. The proposer suggests a lead-time of at least one calendar month would be required for implementation of the Modification Proposal if so directed.

Corona accepted the need for a one month lead time for implementation. SGN also supported implementation within on calendar month.

16. 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.

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

At the Modification Panel meeting held on 15 June 2006, of the 9 Voting Members present, capable of casting 10 votes, 10 votes were cast in favour of implementing this Modification Proposal. Therefore the Panel recommend implementation of this Proposal.

18. Transporter's Proposal

This Modification Report contains the Transporter's proposal to modify the Code and the Transporter now seeks direction from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

TPD SECTION V: GENERAL

Amend paragraph 3.2.4 to read as follows:

“3.2.4 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 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: ...”

Add new paragraph 3.2.9 to read as follows:

“3.2.9 Where a User’s Code Credit Limit has been revised downwards in accordance with paragraph 3.2.4 (c) above, the Transporter will notify the User accordingly on the next Business Day following the occurrence of the event described in paragraph 3.2.4 (c)

Add new paragraph 3.2.10 to read as follows:

3.2.10 Where the Transporter requires the User to provide additional security, the notice given in accordance with 3.2.9 shall require that such User shall provide to the Transporter, by no later than 17.00 on the second Business Day following the date of such notice, additional surety or security in a form acceptable to the Transporter for an amount notified by the Transporter, such that when applied it will result in the Relevant Code Indebtedness of the User not exceeding 100% of the Users Code Credit Limit. Where a User has not provided such additional surety or security by such second Business Day then with effect from the next Business Day next following such second Business Day the following shall be payable by the User:

(a) such amount as set out in the table below based upon the amount of additional surety or security demanded by the Transporter; and

Amount of additional security required	Amount
Up to £999.99	£40
£1,000 to £9,999.99	£70
£10,000 or more	£100

(b) a daily charge equivalent to that percentage rate as is set out from time to time in the Late Payments of Commercial Debts (Interest) Act 1998 multiplied by the amount of additional security demanded by the Transporter.

Subject Matter Expert sign off:

I confirm that I have prepared this modification report in accordance with the Modification Rules.

Signature:

Date :

Signed for and on behalf of Relevant Gas Transporters:

Tim Davis
Chief Executive, Joint Office of Gas Transporters

Signature:

Date :