

Draft Modification Report
Reduction of lapse periods in respect of Failure Notices issued in respect of Energy
Balancing Credit
Modification Reference Number 0143

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

Following the Termination of two Users during the winter of 2005/6, the Energy Balancing Credit Committee (EBCC) carried out a review of events to identify potential areas where controls could be further tightened in pursuit of minimising the community's exposure to financial loss as a result of Energy Balancing Credit Risk.

In an attempt to limit avoidable financial loss, Modification Proposal 0102 "Removal of Failure Notices in respect of Energy Balancing Credit" was proposed but subsequently rejected by the Authority.

This Proposal now aims to address the concerns, highlighted by the Authority in its rejection notice, but still aims to mitigate the concerns raised by EBCC. Reducing the lapse time period between the issuing of failure notices to an optimum level, would still provide the opportunity to notify the Defaulting User that it have infringed Code provisions yet still provide efficient escalation to EBCC.

The scope of this Proposal includes notices in respect of the following areas:

Failure to Pay Cash Call Notice (X2.9.1), Failure to Supply Further Security Notice (X2.10.9) and Failure to Pay Energy Balancing Invoices (X3.2).

The Uniform Network Code currently sets out the following timescales:

Failure to Pay Cash Call Notice

Where National Grid NTS submits a Cash Call notice, and the User does not successfully appeal against such notice, the User is obliged to make payment in full of the Cash Call amount on the Business Day following the Day on which the Cash Call was made. Where payment is not made, Uniform Network Code (UNC) Section X 2.9.1 states that "National Grid NTS shall be entitled to, and as soon as reasonably practicable after the Business Day will, submit to the User a notice substantially in the form set out in the Energy Balancing Credit Rules, notifying the User that National Grid NTS may give Termination Notice to the User if the User does not pay the amount of the Cash Call in full by the Business Day following such notice".

Lapse time in respect of Cash Call Notices was reduced from three to one Business Day as a result of Transco Network Code Proposal 0737 "Failure to Pay cash call Notice (reduced timescales) and has been in operation since 23/03/05. Members believe that this process currently operates at its optimum level. This is supported by statistical data published via the EBCC demonstrating that, since its implementation, there has not been an increase in the number of failures, nor have failures that have been escalated, since implementation of this Proposal, resulted in the issue of a

Termination Notice to the Defaulting User without due consideration of the EBCC. With this in mind, members believe this demonstrates that reduction in financial risk and increased operational controls would be gained as a result of reducing the lapse time in respect of the issue of failure notices in respect of Further Security Requests and the payment of Energy Balancing Invoices. Details of these are outlined below:

Failure to Supply Further Security Notice

Where National Grid NTS submits a Further Security Request and the User has not demonstrated that it is inappropriate to provide further, additional or revised Security and where on the 8th Business Day following such request the User has not complied, UNC Section X 2.10.9 states that “National Grid NTS shall submit to the User a Failure to Supply Further Security Notice in a form set out in the Energy Balancing Credit Rules. Without prejudice to paragraph 1.2.5. National Grid NTS shall notify the Energy Balancing Credit Committee that such notice has been issued.”

UNC provides a further period of seven Business Days before National Grid NTS shall be entitled to issue a Termination Notice to the defaulting User. It also obliges National Grid NTS to convene a meeting of the EBCC to determine if such notice should be issued.

It is proposed that this now be reduced from seven Business Days to one Business Day.

Failure to Pay Energy Balancing Invoice

Where a User fails to pay the net amount of an Energy Balancing Invoice in full on the due date, UNC section X3.2.1 states “ National Grid NTS shall be entitled to, and as soon as reasonably practicable after the Invoice Due Date will, submit to the User a notice, substantially in the form set out in the Energy Balancing Credit Rules, notifying the User that National Grid NTS will give Termination Notice to the User if the User does not pay the outstanding amount of the Net Invoice Amount in full by the 5th Business Day after the date of such notice.”

It is also proposed that the lapse period should be reduced from five Business Days to one Business Day.

Following members detailed review of the circumstances and events leading to and subsequent to Termination Notices being issued to Reepham Limited and Utilita Gas Shipping Ltd in December 2005 and January 2006 respectively, together with the submission of Modification Proposal 0102, its representations and the Authority’s subsequent rejection, EBCC members still believe that the lapse periods in respect of such notices outlined above represent an unnecessary delay presenting avoidable potential financial exposures to the community. This Proposal still aspires to reduce these lapse periods providing National Grid NTS more rapid escalation to EBCC to determine issue of Termination Notices to Defaulting Users in an attempt to curtail the community’s exposure but maintains the safeguard that the Authority believes Modification Proposal 0102 lacked by ensuring the Defaulting User is aware that it has infringed the provisions of the UNC.

Suggested Text

UNIFORM NETWORK CODE – TRANSPORTATION PRINCIPAL DOCUMENT

SECTION X – ENERGY BALANCING CREDIT MANAGEMENT

Amend paragraph 2.10.10 and 2.10.12 to read as follows

- 2.10.10 Subject to paragraph 2.10.12, where the User has not provided the further, additional or revised Security in accordance with the Further Security Request by 12:00 hours on the **following** ~~7th~~ Business Day following the date the Failure to Supply Further Security Notice was submitted and irrespective of the User's Outstanding Relevant Code Indebtedness as at any Day after the submission of the Further Security Request, National Grid NTS shall be entitled to, and as soon as reasonably practicable thereafter may, give Termination Notice to the User (for the purposes of Section V4.3.3) to the effect that the User shall cease to be a User with effect from the Day following the date of the Termination Notice and National Grid NTS shall send a copy of any notice given under this paragraph 2.10.10 to the Authority.
- 2.10.12 Before National Grid NTS shall take the action envisaged by paragraph 2.10.10, National Grid NTS shall convene a meeting of the Energy Balancing Credit Committee as soon as reasonably practicable on or after the **following** ~~7th~~ Business Day following the date the Failure to Supply Further Security Notice was submitted and shall consult with the Energy Balancing Credit Committee to determine whether National Grid NTS should be obliged to issue the Termination Notice, pursuant to paragraph 2.10.10, or whether National Grid NTS should defer taking such step.

Amend paragraph 3.2 to read as follows

- 3.2 **Failure to make payment**
- 3.2.1 Where a User does not pay the Net Invoice Amount under an Energy Balancing Invoice in full on the Invoice Due Date, notwithstanding Section V4.3.1(a) National Grid NTS shall be entitled to, and as soon as reasonably practicable after the Invoice Due Date will, submit to the User a notice, substantially in the form set out in the Energy Balancing Credit Rules, notifying the User that National Grid NTS will give Termination Notice to the User if the User does not pay the outstanding amount of the Net Invoice Amount in full by the **following** ~~5th~~ Business Day after the date of such notice.
- 3.2.2 Where National Grid NTS has given notice to a User under paragraph 3.2.1 and the User has not paid the outstanding amount of the Net Invoice Amount in full by the **following** ~~5th~~ Business Day following the date of such notice, National Grid NTS shall be entitled to and, subject to paragraph 3.2.5, as soon as reasonably practicable after such ~~1st~~ ~~5th~~ Business Day may, give Termination Notice (for the purposes of Section V4.3.3) to the User to the effect that the User shall cease to be a User

with effect from the Day following the date of the Termination Notice.

3.2.3 National Grid NTS will send a copy of any notice given under paragraph 3.2.1 or 3.2.2 to the Authority and without prejudice to paragraph 1.2.5, will notify the Energy Balancing Credit Committee that such a notice has been issued.

3.2.4 Where:

(a) National Grid NTS has given notice to a User under paragraph 3.2.1, and until the Net Invoice Amount under the relevant Energy Balancing Invoice is paid in full; or

(b) a User is a Defaulting User

National Grid NTS will not pay and (irrespective of the Invoice Due Date) shall be entitled to withhold payment pursuant to any Energy Balancing Invoice in respect of, any amounts payable to the User in respect of Energy Balancing Charges ("**relevant amounts**") (and no interest shall accrue and be payable on any such amounts from the Invoice Due Date until the day on which the payment is made) and National Grid NTS shall instead pay the relevant amounts into the User's Cash Call Account.

3.2.5 Before National Grid NTS shall take the action envisaged by paragraph 3.2.2, National Grid NTS shall convene a meeting of the Energy Balancing Credit Committee as soon as reasonably practicable on or after the 1st ~~5th~~ Business Day following the date of the notice given to the User pursuant to paragraph 3.2.1 and shall consult with the Energy Balancing Credit Committee to determine whether National Grid NTS should be obliged to issue the Termination Notice pursuant to paragraph 3.2.2, or whether National Grid NTS should defer taking such step.

2 **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;*

Implementation would be expected to either reduce the extent by which a User would be out-of-balance on the Days following the issue of a Failure to Pay Cash Call Notice, or would reduce the period over which a User that is unable to balance its portfolio is able to continue to participate in the market. These outcomes would be expected to reduce the extent and/or duration of National Grid NTS' actions as the residual system balancer and hence facilitate the achievement of this 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...*

The EBCC (Energy Balancing Credit Committee) concluded that making the proposed revision to the rules governing the management of Energy Balancing Credit

Management would be expected to reduce the level of risk faced by Users. The revisions proposed therefore demonstrate continued development of the objectives of the EBCR (Energy Balancing Credit Rules), namely to “develop and maintain a Framework for limiting the risk of financial loss to the shipper community resulting from the operation of the Energy Balancing regime, at the same time mitigating the avoidable socialisation of avoidable financial loss”. Reducing the risk of financial loss to the Shipper community resulting from the operation of the Energy Balancing regime would be expected to facilitate the securing of effective competition between Shippers and hence implementation of the Modification Proposal would be expected to facilitate achievement of 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.*

Following review of Section X of the Uniform Network Code and the EBCR, the EBCC concluded that implementation of the measures identified within this Modification Proposal would help to ensure that robust procedures and best practice measures are in place to minimise the impact on the industry of User failure and hence would better facilitate the achievement of this relevant objective.

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

More timely curtailment of a User that is unable to balance its portfolio is likely to benefit security of supply.

No implications have been identified in respect of 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:

More timely termination of a User that is unable to balance its portfolio would reduce the number of Days that National Grid NTS would need to carry out consequential residual balancing actions.

b) development and capital cost and operating cost implications:

A reduction in balancing costs would be expected to reflect a reduction in the extent and/or duration of residual balancing actions resulting from a User’s inability to balance its portfolio.

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

Any reduction in residual balancing costs would be reflected in Energy Balancing Neutrality.

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

No such consequences 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 might reduce the contractual risk of Transporters under the Code due to more timely termination of a User.

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 such implications have been identified.

7 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 such implications have been identified.

Development and capital cost and operating cost implications

Implementation would be expected to lead to reductions in Energy Balancing costs in the Days preceding a User Termination.

Consequence for the level of contractual risk of Users

Reductions in contractual risk for other Users would be expected due to more timely Termination of a User.

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

A reduction in the timescale preceding User Termination would lead to non-affiliated Suppliers and consumers having to establish new supply arrangements earlier than otherwise.

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 have been identified.

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

Advantages

- curtails exposure to avoidable financial loss
- reduces lapse time periods to a more optimum level
- continues to provide both the opportunity and appropriate safeguards to ensure a proportionate and fair response to credit infractions.

Disadvantages

None identified

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

Representations are now invited

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

No such requirement has been identified.

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

No such requirement has been identified.

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

No programme for works has been identified as being required as a consequence of implementing the Modification Proposal.

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

It is recommended that this Proposal be implemented immediately following the decision by the Authority.

It is assumed that if any User were in receipt of any notices, encompassed by this Proposal, at the date of implementation, revised notices would be served on that User that reflected, as far as was practicable, the amended timescales.

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

No such implications have been identified.

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

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 and Electricity Markets Authority in accordance with this report.

19 Text

The Modification Panel did not determine that text was required for inclusion in this Modification Report. However, suggested text has been provided as part of the Proposal (see section 1 above).

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