

CODE MODIFICATION PROPOSAL No. 0145
Management of Users Approaching and Exceeding Code Credit Limit
Version 1.0

Date: 04/05/2007

Proposed Implementation Date: 01/12/2007

Urgency: Non Urgent

1 The Modification Proposal

a) Nature and Purpose of this Proposal

In respect of transportation credit arrangements, Ofgem published a number of recommendations in its conclusions document “Best practice guidelines for gas and electricity network operator credit cover” 58/05 in February 2005.

Pursuant to recommendations contained within the conclusions document it is proposed that where a User’s Value at Risk (VAR) reaches 80% of the value of the Code Credit Limit (CCL), the Transporter issues a warning notice to the User (which would not be accompanied by calls for additional security or the disconnection of existing customers and/or inhibiting the registration of new customers). Whilst the conclusions document advocated that this notice is issued at 85%, National Grid Distribution believes that implementation efficiencies for Transporters can be achieved if this notice is issued at 80%. This level of Value at Risk is a key point in other aspects of the proposed credit arrangements and given that no sanctions are applied at this level (it merely being a notice) this would not appear to be a significant deviation from the conclusions document. It is proposed to remove the current notice requirements and availability of sanctions at 70% and 85% Relevant Code Indebtedness (as a percentage of the Code Credit Limit) respectively.

It is proposed that the current measures available to Transporters (pursuant to UNC TPD section V3.3.2) are only available where a User’s VAR exceeds 100% of its CCL. The measures being the entitlement for the Transporter to reject:

- an application for System Capacity or increased System Capacity,
- a System Capacity Trade, or
- a Supply Point Nomination or Confirmation (subject to the following proposed provisions).

It is further proposed that where a User’s VAR exceeds 100% of the value of the CCL in place, the User be required (by a notice issued to the User on the following Business Day) to provide additional security within two Business Days of the date of the notice sufficient to reduce the User’s VAR below 100% of the CCL. Where the additional security is provided after the

two business days identified above, the value of this additional security would be required to be sufficient to reduce the User's VAR to 80% of the CCL. For the following 12 month period, the value of the security in place will be deemed to be 80% of its normal value.

It is further proposed to incorporate within the UNC provisions concerning remedies for instances where a User fails to provide additional security (where a User's VAR exceeds its CCL) following a notice issued by the Transporter. Where such additional security is not forthcoming, the Transporter would claim liquidated damages in line with the Late Payment of Commercial Debts (Interest) Act 1998 based on the value of the additional security outstanding.

The above sanctions will be applied in accordance with the following timetable:

Number of Business Days relative to expiry of notice	Action
-2	Notice issued. Sanctions available to Transporter: ability to reject an application for System Capacity (or an increase in such) or a System Capacity Trade
0	Expiry of notice (2 business days following date of issue)
1	Liquidated damages trigger (in line with Late Payment of Commercial Debts (Interest) Act 1998). Transporter issues statement of position to User and confirms how default is to be remedied.
3	Formal User response required
5	Sanction available to Transporter to suspend registration of Supply Points (Supply Point Nomination and Confirmation)

It is further proposed that where a User experiences a material change to its level of trade (detected via monitoring of a VAR) as a consequence of an increase in the relevant Transporter's transportation charges, a notice period of one month will be allowed for the User to post any additional security required. A 'material change' will be an increase in the User's VAR of 20% or greater from the previous day.

UNC Transportation Principal Document Section V3.3.3 currently entitles the Transporter to give Termination Notice where Relevant Code Indebtedness exceeds 100% of the User's CCL. It is further proposed to amend this provision to reflect that this entitlement alternatively applies where a User's VAR exceeds 100% of the User's CCL.

If this Proposal is not implemented, UNC will not reflect the recommendations contained within the Ofgem conclusions document and Transporters will not be obliged to operate this aspect of their credit arrangements in a consistent manner.

b) Justification for Urgency and recommendation on the procedure and timetable to be followed (if applicable)

N/A

c) Recommendation on whether this Proposal should proceed to the review procedures, the Development Phase, the Consultation Phase or be referred to a Workstream for discussion.

This Modification Proposal has been developed within the Uniform Network Code (UNC) Distribution Workstream. General consensus on its objectives was forthcoming. 'Proceed to consultation' is therefore requested.

2 Extent to which implementation of this Modification Proposal would better facilitate the achievement (for the purposes of each Transporter's Licence) of the Relevant Objectives

Implementation of consistent credit processes which move towards recognised best practice would help ensure that there is no inappropriate discrimination and no inappropriate barrier to entry. This measure facilitates the securing of effective competition between relevant shippers.

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

No such implications on security of supply or operation of the Total System have been identified. Incorporating elements of credit rules within the UNC may help to reduce the impacts of any industry fragmentation.

4 The implications for Transporters and each Transporter of implementing this Modification Proposal, including:

a) The implications for operation of the System:

No implications for operation of the system have been identified.

b) The development and capital cost and operating cost implications:

The Proposer believes that significant changes would be required in respect of operational processes and procedures in the event of implementation of this Modification Proposal which will incur development costs in adjusting trigger levels for sanctions and creating processes and procedures to enable compliance with the provisions of this proposal. An equivalent increase in operating cost may transpire in the prospective operation of the new provisions that would be introduced.

c) Whether it is appropriate to recover all or any of the costs and, if so, a proposal for the most appropriate way for these costs to be recovered:

No cost recovery mechanism is proposed.

d) The consequence (if any) on the level of contractual risk of each Transporter under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

Removal of measures which a Transporter is currently able to apply at the point a User exceeds 85% indebtedness under UNC section V3.3.2 will increase Transporters level of contractual risk.

Where a Transporter is able to demonstrate that it has implemented credit control, billing and collection procedures in line with the Guidelines, it may be in a position to secure pass through of any bad debt it incurs. In such cases, Ofgem clarified in its Best Practice Guidelines that at the subsequent price control review the Transporter will be permitted to raise up to the full value of the bad debt from regulated charges including an allowance for the cost of funding the loss pending recovery. Where a Transporter is able recover bad debt incurred this mitigates the Transporter's increased contractual risk associated with implementation of aspects of the Best Practice Guidelines.

5 The extent to which the implementation is required to enable each Transporter to facilitate compliance with a safety notice from the Health and Safety Executive pursuant to Standard Condition A11 (14) (Transporters Only)

Implementation is not required for such.

6 The development implications and other implications for the UK Link System of the Transporter, related computer systems of each Transporter and related computer systems of Users

No UK Link systems implications have been identified.

7 The implications for Users of implementing the Modification Proposal, including:

a) The administrative and operational implications (including impact upon manual processes and procedures)

Users may be required to amend operational processes to address the new triggers for notices and requests received from the Transporter to rectify its credit security position.

b) The development and capital cost and operating cost implications

Where a Transporter obtains approval to pass through bad debt, this is likely to be subsequently reflected in increased Transportation Charges which would be payable by Users in the subsequent price control period.

c) The consequence (if any) on the level of contractual risk of Users under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

Where a User's Value at Risk is between (in excess of) 85% and 100%, its level of contractual risk will reduce as the measures pursuant to Section 3.3.2 will not be available to Transporters. Where indebtedness exceeds 100%, Users would potentially be exposed to additional financial risk (associated with charges levied in accordance with the Late Payments of Commercial Debts (Interest) Act 1998). This risk can be avoided by rectification of the credit security position within the required timescale.

8 The implications of the implementation for other relevant persons (including, but without limitation, Users, Connected System Operators, Consumers, Terminal Operators, Storage Operators, Suppliers and producers and, to the extent not so otherwise addressed, any Non-Code Party)

Dependent on the contractual arrangements in place between the respective parties, bad debt costs which are reflected in subsequent Transportation Charges may be borne in part or in full by Suppliers and subsequently consumers.

9 Consequences on the legislative and regulatory obligations and contractual relationships of the Transporters

Where a Transporter secures pass through of any bad debt it incurs and demonstrates that a delay in recovery would have a material adverse effect on its financial position, Ofgem clarified in its Best Practice Guidelines that it may consider early licence modifications such that amounts can be recovered prior to the next price control period.

10 Analysis of any advantages or disadvantages of implementation of the Modification Proposal not otherwise identified in paragraphs 2 to 9 above

Advantages

- Alignment with Best Practice Guidelines.
- For a User with a Code Credit Limit 'usage' of in excess of 85% Relevant Code Indebtedness, exposure to the measures available to Transporters pursuant to Section V3.3.2 will be removed until, under the proposed arrangements the User's Value at Risk exceeds 100%.
- Users would be able to utilize the full extent of its credit security without sanction.

Disadvantages

- For Transporters no practical measures will be available to mitigate exposure where a User's Value at Risk exceeds 85% (and does not exceed 100%).
- For Users, if a Transporter can demonstrate compliance with Best Practice Guidelines (of which this is one element), Users may be subject to a level of financial risk of bad debt incurred by the Transporter.

11 Summary of representations received as a result of consultation by the Proposer (to the extent that the import of those representations are not reflected elsewhere in this Proposal)

No representations have been invited at this stage.

12 Detail of all other representations received and considered by the Proposer

No such representations have been received.

13 Any other matter the Proposer considers needs to be addressed

No such additional matters (related with this proposal) have been identified.

14 Recommendations on the time scale for the implementation of the whole or any part of this Modification Proposal

In light of the work required, the Proposer believes that this Modification Proposal could be implemented with effect from 3 months following the appropriate direction being received from the Authority.

15 Comments on Suggested Text

None.

16 Suggested Text

TPD SECTION V: GENERAL

Amend paragraph 3.2.10 as follows:

3.2.10 Where the Transporter...not exceeding 100% of the User's Code Credit Limit. Subject to paragraph 3.2.11 below, where a User has not provided...payable by the User...

Add new paragraph 3.2.11 as follows:

3.2.11 Notwithstanding paragraph 3.2.10, where at any time as a direct consequence of an increase in the relevant Transporter's Transportation Charges, a User's Value at Risk is increased by over 20% from the previous day, a User will have one calendar month from the date of notice given by the relevant Transporter to provide additional surety or security and after the expiry of such date, paragraphs 3.2.10 (a) and (b) shall apply.

Delete title of paragraph 3.3 and replace with the following:

"Requirements as to Value at Risk"

Delete paragraph 3.3.1 and replace with the following:

3.3.1 Where:

(a) a User's Value at Risk exceeds 80% of its Code Credit Limit and the

Transporter has given notice to the User to that effect; and

- (b) at any time following any notice given pursuant to (a) above, the User's Value at Risk exceeds 100% of its Code Credit Limit, the Transporter will notify the User of such event, giving such User 2 Business Days from the date of such notice to provide additional surety or security for the amount specified by the Transporter in the notice in order to reduce its Value at Risk to below 100% of its Code Credit Limit.

Delete paragraph 3.3.2 and replace with the following:

3.3.2 Without prejudice to paragraph V3.3.3, where a User fails to provide such additional security as required in paragraph 3.3.1 (b) by the date specified in the notice pursuant to 3.3.1(b):

- (a) the amount of such surety or security required shall be increased to that amount required to reduce the User's Value at Risk to below 80% of its Code Credit Limit and any surety or security provided by such User shall be deemed to be valued at 80% of its face value for the following 12 calendar months; and
- (b) with effect from the next Business Day after the date specified in such notice, the User shall pay to the Transporter that amount set out in the table in paragraph 3.2.10(a), based upon the amount of additional surety or security demanded by the Transporter and the daily charge set out in paragraph 3.2.10(b); and
- (c) subject to paragraph 3.3.1, where and for so long as the User's Value at Risk exceeds 100% 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:
 - (i) an application for System Capacity or increased System Capacity at any System Point under Sections B or G5; and/or
 - (ii) in relation to the NTS, a System Capacity Trade under Section B5 in respect of which the User is Transferee User;

until such time as the User's Value at Risk is reduced to less than 100% of its Code Credit Limit.

- (d) where from the fifth Business Day after the date specified in the notice, the User's Value at Risk exceeds 100% of the User's Code Credit Limit, the Transporter shall be entitled to reject or refuse to accept a Supply Point Nomination or Supply Point Confirmation under Section G, other than a Supply Point Renomination or Supply Point Reconfirmation until such time as the User's Value at Risk is reduced to less than 100% of its Code Credit Limit.

Delete paragraph 3.3.3 and replace with the following:

3.3.3 Subject to paragraph 3.3.1, where and for so long as the Value at Risk of the

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.

Code Concerned, sections and paragraphs

Uniform Network Code

Transportation Principal Document

Section(s) V

Proposer's Representative

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