

Modification proposal:	<b>Uniform Network Code (UNC) 190: Clarification of Aggregate Credit Positions using a guarantee from a Security Provider</b>		
Decision:	The Authority <sup>1</sup> directs that this proposal be made		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	6 June 2008	Implementation Date:	To be confirmed by the Joint Office

## Background to the modification proposal

In October 2007, the Authority approved UNC modification 0148. The intention of that modification was to allow a Parent Company Guarantee (PCG) or a guarantee provided by an Independent Security Provider (ISP) to be used in one of two ways:

1. That the unsecured credit limit assigned to the User would be based on the credit strength of the parent guarantor. Thus for example, a BB rated User guaranteed by an A rated parent would obtain an unsecured limit equal to 40 per cent of the relevant Transporter's maximum credit limit. Where more than one User obtains credit from a single PCG, the aggregate counterparty credit limits (obtained via that PCG) shall not exceed the credit entitlement of the parent.
2. As a guarantee for an amount in addition to an Unsecured Credit Limit assigned to the User based on its stand alone credit rating. In such a case, the additional amount secured by the parent must not exceed the parent company's ability to bear risk and must take into account the extent to which other Users are secured by the parent under the UNC.

It was the proposer's view however that the modification did not give sufficient clarity for the use of a PCG or an ISP as envisaged under point 2.

## The modification proposal

The proposal seeks to clarify that a Guarantee provided by a PCG or ISP also allows a User to enhance the overall credit rating in a manner that is incremental to the User's existing unsecured credit limit obtained of its own accord.

The proposer is of the view that the implementation of this change will better facilitate the achievement of the relevant objective in standard special condition A11.1(d) viz "the securing of effective competition:

- (i) between relevant shippers;
- (ii) between relevant suppliers; and/or
- (iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers."

It is their view that competition between users would be enhanced because implementation of clear and consistent credit processes would help ensure that there is no inappropriate discrimination and no inappropriate barrier to entry. Therefore, the proposer considers that this measure facilitates the securing of effective competition

<sup>1</sup> The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

between relevant shippers.

The user has modified the text of their proposal to make clear that the acceptance of a Guarantee used to incrementally increase the level of credit of a User over and above that which it could obtain of its own accord will be subject to the discretion of the Network Operator who will assess the overall ability of the credit support provider to bear the risk in the event of a default.

### **UNC Panel<sup>2</sup> recommendation**

At the Modification Panel meeting held on 21 February 2008, of the 9 Voting Members present, capable of casting votes, 9 votes were cast in favour of implementing this Modification Proposal. Therefore the Panel recommend implementation of this Proposal.

### **The Authority's decision**

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 21 February 2008. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR<sup>3</sup>. The Authority has concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC<sup>4</sup>; and
2. directing that the modification proposal be made is consistent with the Authority's principal objective and statutory duties<sup>5</sup>.

### **Reasons for the Authority's decision**

We consider that provided the arrangements are sufficiently robust and unconditional, Users should be permitted to use credit cover tools available to them in the most flexible manner as possible.

To this end, we did have some concern that the use of a Guarantee, particularly from a parent should not create a situation where the overall level of risk is greater than the corporate group together is able to bare. We consider this proposal introduces sufficient safeguards in to the process to ensure that this should not occur.

In particular 3.1.6 c states:

"Where a Security Provider provides security pursuant to paragraph 3.1.6 b or d for more than one user the aggregate security provided by the Security provider shall not exceed the maximum credit entitlement of the Security Provider calculated in accordance with the table set out in paragraph 3.1.6 a."

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<sup>2</sup> The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules

<sup>3</sup> UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at [www.gasgovernance.com](http://www.gasgovernance.com)

<sup>4</sup> As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: [http://epr.ofgem.gov.uk/document\\_fetch.php?documentid=6547](http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547)

<sup>5</sup> The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986.

The Authority considers this correctly limits the total credit risk which a user or aggregate of affiliated users can obtain.

The proposer has amended paragraph 3.1.6 d to state

“(d) A User may increase an Unsecured Credit Limit allocated pursuant to paragraph 3.1.6(a) or paragraph 3.1.7 by an incremental amount (the "Incremental Amount") by providing security (in respect of the Incremental Amount) in the form of a Guarantee from a Security Provider with an Approved Credit Rating subject to:

- (i) such Approved Credit Rating being sufficient to cover the Incremental Amount as calculated in accordance with the table set out in paragraph 3.1.6(a); and
- (ii) paragraph 3.1.6(c); and
- (iii) in the opinion of the Transporter, such Security Provider’s ability to bear risk not being exceeded.”

Ofgem is of the view that the safeguards outlined above are therefore, at present, sufficiently robust to ensure that the risk taken on by the credit support provider should not be greater than any risk it itself would be able to incur. Ultimately, where the Transporter is not satisfied that the security provider can bear the risk then it has the discretion to not extend the incremental or increased level of credit. In such circumstances we consider allowing the transfer of risk from the User to the credit support provider to better facilitate the achievement of relevant objective (d), allowing Users to benefit from a superior credit rating of a credit support provider or increase their own available credit but to an appropriate incremental level

Considering the issues outlined above Ofgem is of the view that this proposal does better facilitate relevant objective (d) of the UNC.

#### **Decision notice**

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority, hereby directs that modification proposal UNC 190: *Clarification of Aggregate Credit Positions using a guarantee from a Security Provider* be made.



**Stuart Cook,**  
**Transmission Director, Networks.**

Signed on behalf of the Authority and authorised for that purpose.