CODE MODIFICATION PROPOSAL No 0315
To Enhance Section X of the UNC Transportation Principal Document to improve the Energy Balancing Further Security Process
Version 2.0

Date: 29/07/2010

Proposed Implementation Date:

Urgency: Non Urgent

1 The Modification Proposal

a) Nature and Purpose of this Proposal

Background

The Energy Balancing Credit Committee (EBCC) keeps under constant review the credit arrangements in Section X of the UNC Transportation Principal Document. It has identified a weakness in the existing rules in respect of Further Security Requests. Further Security Requests are raised following a number of breaches of a User's Secured Credit Limit.

Modification 629 implemented 14th May 2003 introduced provision to the UNC in respect of Further Security Requests, its primary aim being to encourage Users to maintain the appropriate level of Security to cover its Energy Balancing activities. Following operation of these provisions since this time, analysis of the number of instances of such requests has evidenced an issue in respect of repeated failures. Some Users have received a number of Further Security Requests within a short period of time demonstrating that insufficient Security is held.

The rules currently do not prevent a User from simply 'topping up' their Security to meet their short term requirements. This means that where a User is running a persistent imbalance the Energy Balancing Rules do not act as adequate incentive to ensure that the User maintains the appropriate level of Security to accommodate the level of their Energy Balancing activities and avoid repeated Cash Calls and Further Security Requests.

The EBCC considered various solutions to this problem. On the 23rd October 2009 the EBCC met and agreed this proposed solution as the most appropriate. Corona Energy agreed to adopt the proposal and raise it as a UNC modification.

The proposal aims to extend the provisions of Section X2.10 to make provision for the utilised value (Cash Call Limit) of the User's existing Security held to be scaled back by a percentage, initially proposed to be 20%, to act as an incentive to break the cycle of repeated failure through the Cash Call and resulting Further Security Request process. Further it aims to incentivise the User to maintain the correct level of Security to accommodate the level of its Energy Balancing activities.

It is further proposed that the provisions of Section X2.4 and X2.2 be amended to provide for the relationship between the User's Cash Call Limit

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and Secured Credit Limit to be revised to facilitate such scale back.

The EBCC credit experts discussed various levels of scale back that could be implemented. There was unanimous agreement that a level of 20% was the most appropriate as it was believed to be a sufficient incentive without being punitive. It was also recognised however that this level would require monitoring and could require changing in the future if evidence suggested the level was set too high or too low.

The Proposal

The current provisions require the User to maintain Security at the peak level of indebtedness for a period of no less than 90 Days from the date of any FSR issued (providing that conditions of UNC Section 2.3.5 have been met). It is proposed to extend the provisions in Section X2.10 so that the utilised value (User's Cash Call Limit) of the User's Security will be scaled back by a percentage (initially to be set at 20%) as soon as is reasonably practicable following the 3rd FSR within the 28 day measurement period. The resulting revised Cash Call Limit will remain in place for a minimum period of 12 months (re-basing period).

Any 3rd FSR in a new '28 day measurement period' that takes place within the duration of the 're-basing period' will trigger a further percentage reduction (again initially proposed to be 20%) in the User's Cash Call Limit and a new re-basing period' will commence.

Once any re-basing period' has expired and the User has not had any further FSRs, a subsequent Cash Call will commence a new '28 day measurement period'.

Once any re-basing period' finishes, without any further re-basing periods' being triggered, any Security held may be returned at the User's request providing that conditions of UNC Section x2.3.5 have been met and the User's Cash Call Limit is revised accordingly.

The Proposer believes that this proposed change draws on the learning from Transportation Credit Arrangements where similar actions are taken in accordance with V 3.3.2 where a User fails to comply with a request for increased Security within a defined period of time.

In order to facilitate the scale back it is further proposed that the provisions of section X2.4 and X2.2 be amended to provide for the relationship between the User's Cash Call Limit and Secured Credit Limit to be revised.

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The simple example in the table below aims to demonstrate how this would operate in practice by using £100 as the value of Security provided by the User.

Users Security	Cash Call Limit	Proposed Scale Back	Revised Cash Call Limt
£100	£85 i.e 85% in accordance with prevailing rules x 2.4	20%	£68
£100	£68	20%	£54.40
£100	£54.40	20%	£43.52
£100	£43.52	20%	£34.82
£100	£34.82	20%	£27.86

NB: Please note a more detailed example has been attached that shows the effect of implementation of this modification where a User is running a persistent imbalance on its inputs and outputs and this results in repeated Cash Calls and FSR's. (Appendix 1 V2)

For the avoidance of doubt, this proposal does not affect the Users right to appeal a FSR or Cash Call via existing processes, but introduces a new right of appeal to challenge the calculation of the revised Cash Call Limit. Further it should be noted that this proposal does not affect National Grid NTS's ability to consult the EBCC in relation to any function required under section X of the code in the event that a User is unable to satisfy the requirements of the revised processes proposed.

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

No Urgency required.

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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.**

To progress to Consultation.

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2 User Pays

a) Classification of the Proposal as User Pays or not and justification for

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classification

There are no additional xoserve operating costs associated with this Modification proposal as provisions for charging is within the Agency Service Agreement. Were any costs to be identified then it is proposed that this modification should not be user pays as it relates to a service that is provided under the GT's licence and is therefore a core service.

b) Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification

Under prevailing Energy Balancing Arrangements it is believed that the cost associated for the recovery, provisions are within the Agency Service Agreement. Were this not to be the case then it is proposed that the costs of this modification should be borne initially by the GT and recovered through the neutrality smear in line with other costs that relate to Energy Balancing credit such as credit checking such as banking charges.

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c) Proposed charge(s) for application of Users Pays charges to Shippers

Not applicable

d) Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from xoserve

Not applicable

3 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

c. so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;

We believe that this change will enhance the Gas Transporter's compliance with Standard Special Condition A15 "Agency".

Section 3 states that where these services are provided by a common service provider the contract with this agent shall be based on the following principles

(i) "such services and systems shall be established, operated and developed on an economic and efficient basis."

This change will have little or no cost impact but will improve the performance of the process by minimizing the financial risk to other code Users of another User defaulting. This change therefore improves the economy of the process.

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d. so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition between relevant shippers and between relevant suppliers;

Implementation of this Modification would (in comparison to the existing process) affect a User who is repeatedly cash called within a 28 day measurement period and therefore receives 3 or more Further Security Requests. This User would either be required to provide a greater level of Security or would fall below their Cash Call Limit and would be referred to the EBCC to solve their credit issues (see attached example in Appendix 1 v2).

Either of these outcomes would reduce the risk to other code Users of the failure of a single code User. This minimises the financial risk to Users and therefore reduces the costs of being active in the gas shipping market.

The EBCC believes however that Users would be aware of the rules and upon receipt of a second FSR, would provide sufficient Security rather than risk a 20% reduction in the utilised value of their security (Cash Call Limit) . This change would therefore act as an incentive against the 'topping up' behaviour previously described.

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

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

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

a) The implications for operation of the System:

No implications have been identified.

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

No costs identified.

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 costs have been identified. However where any additional costs are identified will be added as a new element to the Balancing Neutrality mechanism based upon additional FTE required to maintain process.

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

No consequences identified.

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6 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)

No such requirements have been identified.

7 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 such requirements have been identified.

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

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

No adverse administrative and operational implications identified. However this will be monitored regularly if implemented and discussed at the EBCC meeting.

b) The development and capital cost and operating cost implications

No development costs identified.

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

This proposal would reduce User's contractual risk as it will reduce the risk of Users defaulting on an unsecured debt.

9 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)

Implication identified would be on Users to provide additional Security where the trigger has been met.

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

No such implications identified.

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

Advantages

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Users will be encouraged to provide adequate Security at all times.

Will maintain Users confidence that risk of default is being managed effectively.

Disadvantages

Adds a level of complexity to the arrangements.

12 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)

None received.

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

The modification has been developed by the EBCC.

14 Any other matter the Proposer considers needs to be addressed

None

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

It is recommended that this proposal be implemented immediately following agreement by Authority.

16 Comments on Suggested Text

Section 2.10.3

17 Suggested Text

Section 2.10.13 Further Security Request

In the event where a User is issued a 3rd Further Security Request within the 28 day measurement period, the User's prevailing Cash Call Limit shall be scaled back by a percentage determined in accordance with the Energy Balancing Credit Rules. A notice in a form set out in the Energy Balancing Credit Rules advising the User of the revised Cash Call Limit will be issued to the User as soon as reasonably practicable following such event, such revised Cash Call Limit shall remain in force for a period of not less than 12 months (re-basing period) from the issue date of the notice.

2.10.14 Where the User considers that the revised Cash Call Limit has been calculated erroneously the User may not later than 12:00 Hours on the Business day following issue of the notice appeal such notice specifying in as much detail as is possible the User's reasons for so considering.

2.10.15 In the absence of an appeal considered in X2.10.14 in the event of any

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subsequent issue of a Further Security Request during the re-basing period the User's Cash Call Limit will again be reduced by a further percentage as determined in the Energy Balancing Credit Rules and a new re-basing period will commence following the issue of a relevant notice.

Section 2.4.1

For each User the Cash Call Limit is the amount determined by National Grid NTS in accordance with the prevailing provisions of the Energy Balancing Credit Rules and section X2.13 not exceeding 85% of the User's Secured Credit Limit, elected by or assigned to the User in accordance with this paragraph 2.4 as the limit on its Outstanding Relevant Balancing Indebtedness.

Section X2.2.3 The amount referred to in paragraph 2.2.2 is the amount for the time being of the Security the User has provided unless the provisions of X2.10 have been applied.

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Code Concerned, sections and paragraphs

Uniform Network Code

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Section(s) X2.2.3, X2.4.1 & 2.10

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Proposer's Representative

Richard Street – Corona Energy Retail

Proposer

Gary Russell – Corona Energy Retail

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