

Draft Modification Report
Right of set off under Uniform Network Code
Modification Reference Number 0076
Version 2.0

This Draft 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 a recommendation identified within Ofgem's conclusion document "*Best Practice Guidelines for Gas and Electricity Network Operator Credit Cover*" 58/05. This concluded the high-level principles that should be applied and further work required in respect of credit cover arrangements for transportation arrangements.

This Proposal seeks to implement recommendations detailed within paragraph 3.49 of the conclusion document.

Under the UNC, Transporters may issue either credit or debit invoices to Users, payable by the Transporter or the User within terms specified in the UNC. Historical data indicates that when considering monies owed between User and Transporter for the normal monthly billing cycle, the User will usually be in debt when the net position is calculated.

It would be beneficial to Transporters if (in respect of Transportation services only) a Transporter had the ability to offset amounts it was due to pay to the User against any invoice value that the User is due to pay the Transporter when a User is in breach of payment terms (UNC Section S3.1) or has agreed with the Transporter the set-off.

This right of set off would therefore only be available where:

- the relevant Transporter was the same party in respect of both the credit and debit amounts, and
- the relevant User was the same party in respect of both the credit and debit amounts, and
- the relevant User is in breach of the relevant payment terms, or has agreed with the Transporter the set-off of the relevant amounts.

In respect of the set off:

- the Transporter would issue a 'set off notice' to the User in instances where a User is in breach of Section S3.1
- the 'set off notice' would specify the relevant invoice payable (or, if applicable the unpaid overdue invoice) by the User and the invoice payable by the Transporter which is being set off on or before the invoice due date.

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

National Grid believes that implementation of this Proposal would represent a reasonable efficiency improvement in respect of the making of payments and is thus consistent with the relevant objective of the promotion of efficiency in the implementation and administration of the Network Code and/or the Uniform Network Code. While implementing set-off could impose costs on Users, the Proposal envisages set-off only being applied with the consent of the User involved such that the benefits would be expected to outweigh the costs.

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

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

No implications on security of supply, operation of the Total System or industry fragmentation have been identified.

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 or capital costs have been provided.

National Grid Distribution “estimates that if a right of set off were...in place...from January 2005 to August 2005, [National Grid] would have had the ability to reduce the quantity of invoices issued by 39%. In addition ...realised a...saving of approximately £6,500 in...banking charges”.

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 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

No such consequence is anticipated.

The SME believes that the level of contractual risk for Transporters is diminished where it is able to set off and utilise credits due to Users to reduce the level of outstanding debt.

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 Transporters.

User systems may need to be amended if they elect to allow set-off.

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

Implementation of the Modification Proposal has the potential to reduce or increase Users' administrative and operational costs. However, since the Proposal allows Users to elect whether or not to allow set-off, net benefits are anticipated.

The SME believes there is potential for a reduction in a Users contractual risk in that where set off is utilised, a Users level of indebtedness is reduced which minimizes the risk of exposure to sanctions which Transporters are able to impose at the levels prescribed by UNC (currently 85%).

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 have been identified

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.
- Potentially reduces industry administration costs.

Disadvantages

- Potentially increases complexity, especially if each of the relevant Transporters act differently

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 sought in respect of this Draft Report and prior to the Transporters finalising the Report

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 in the event that this Modification Proposal is implemented.

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

Changes would be required in respect of operational processes and procedures. A lead-time of at least one month would be required for implementation of the Modification if so directed.

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

19. Text

TPD SECTION S: INVOICING AND PAYMENT

Amend paragraph 3.3.1 to read as follows:

Without prejudice to paragraphs 3.8 and 4.2.2, amounts payable....

Add new paragraph 3.8 to read as follows:

3.8 Set off notice

3.8.1 A Transporter may submit a notice ("**Set off Notice**") to a User in respect of a relevant Invoice Document where either:

(a) such User has failed to make payment in full in respect of such Invoice Document by the Invoice Due Date in accordance with paragraph 3.1; or

(b) such User has agreed in writing that a Transporter may apply set off in accordance with this paragraph 3.8 and such User has not withdrawn such agreement by notice in writing at least 5 Business Days prior to any Set Off Notice;

in such case, the provisions of this paragraph 3.8 shall apply.

3.8.2 For the purposes of this paragraph 3.8 a "**relevant**" Invoice Document is an Invoice Document which:

(a) has been submitted to the User;

(b) comprises Invoice Amounts (including Invoice Amounts under any other relevant Invoice Document specified in the Set off Notice) which are payable both by and to a User; and

(c) such Invoice Amounts are in respect of Transportation Charges.

3.8.3 A Set off Notice shall specify:

(a) the identity of the User;

(b) in respect of each relevant Invoice Document:

(i) the unique number by which the Invoice Document is identified;

(ii) the date the Invoice Document was submitted to the User;

(iii) the Invoice Type;

(iv) the Invoice Due Date;

(v) in respect of each Invoice Item, the Invoice Amount;

(c) by reference to each of the Invoice Amounts payable both by and to a User under each relevant Invoice Document, the net amount payable by or to the User (the "**net invoice amount**"); and

(d) the Invoice Document (the "**specified**" Invoice Document) in respect of which the net invoice amount is to be treated as payable (which in the case of a Set

off Notice in respect of a single Invoice Document shall be such Invoice Document).

3.8.4 Following the submission of a Set off Notice:

- (a) payment of the net invoice amount by the Transporter or (as the case may be) the User on or before the Invoice Due Date of the specified Invoice Document shall be treated for the purposes of this Section S as payment in full of all Invoice Amounts payable by or to the User under each relevant Invoice Document specified in the Set off Notice;
- (b) paragraphs 3.2, 3.4 and 3.7 shall apply in respect of each relevant Invoice Document;
- (c) the Transporter or (as the case may be) the User will remain liable for the payment of interest in accordance with paragraph 3.5 in respect of the late payment of any Invoice Amount under a relevant Invoice Document where payment was not made by the Invoice Due Date; and
- (d) in the event the net invoice amount is not paid on or before the Invoice Due Date of the specified Invoice Document paragraph 3.5 shall apply in respect of each Invoice Document specified in the Set off Notice.

3.8.5 Where a User has notified the Transporter of an Invoice Query (in accordance with paragraph 4.2) in respect of an Invoice Item under a relevant Invoice Document:

- (a) prior to the submission of a Set off Notice, the Transporter shall take account of the Invoice Amount which is the subject of the Invoice Query when determining the net invoice amount payable;
- (b) following the submission of a Set off Notice, the Transporter may:
 - (i) make payment of any such amount for which it is liable pursuant to this Section S in respect of the Invoice Query; or
 - (ii) submit a revised Set off Notice to take account of the Invoice Amount which is subject of the Invoice Query (and the first Set off Notice shall cease to have effect).

Representations are now sought in respect of this Draft Report and prior to the Transporters finalising the Report

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 :