

Terms of Reference v1.0
UNC Modification Reference Number 0221
Review of Entry Capacity and the Appropriate Allocation of Financial Risk

Purpose

This Review Proposal seeks to establish whether or not the current credit arrangements in place for securing Entry Capacity are sufficiently robust and provide the correct balance of risk between various UNC Parties. Where issues are identified this Review Group will seek remedies to resolve them.

Background

The current credit rules within the UNC require that a User puts in place credit arrangements to provide security for the 12 months immediately prior to the start date of the QSEC capacity previously bought in a QSEC auction, which includes the Incremental Capacity Release Obligations. This underwriting timeframe can be misaligned with that of the costs or revenue recovery requirement incurred in meeting the auction obligations. Therefore there is currently a period of time where either of the above could be incurred prior to any commitment underwriting being in place.

As the patterns of gas delivery to the NTS change and the GB market becomes increasingly dependent on overseas gas supplies, significant investment is anticipated to be required in order to develop import and storage facilities. It is also anticipated that a number of these new projects will be developed by participants that are 'new' to the GB gas market and may also be single entry point Users.

In this context, one facet of the existing credit arrangements is that there is potentially an increased risk of User default resulting in increased costs being incurred by other industry stakeholders. The entry capacity incentive arrangements from April 2007 enable National Grid Gas NTS to recover 5 years of incentive payments from the first month that capacity is released based on the revenue driver in the GT Licence. In the event that the relevant User defaults, the incremental obligated entry capacity can be offered for resale. However, any under-recovered revenue driver income would continue to accrue. This would, in turn, lead to the SO commodity charge payable by all Users being increased to recover the short fall in allowed revenue. In effect the shipper community holds a risk associated with the current mismatch between the credit underwriting timeframe currently in the UNC and the timeframe over which investment costs accrue.

National Grid Gas NTS therefore consider it to be prudent for the industry to review the current credit arrangements that underpin User commitments that are made during the entry capacity auctions.

It is therefore proposed that this Review Group be established to:

- review the existing credit security arrangements
- consider the issues which impact upon the relevant objectives including:
 - efficient and effective operation
 - development of competition
 - delivery of licence including no undue discrimination
- develop potential solutions to resolve any issues identified where appropriate
- develop any UNC contractual changes as necessary.

Scope and Deliverables

The Review Group is to consider the following:

- Consider whether the current credit and security arrangements are sufficiently robust to underpin User commitments effectively. For example; lead time, duration, level of credit cover, types of credit mechanisms, type of capacity covered by any new arrangements.
- Consider whether the current arrangements unduly impact existing Users to a greater extent than they do for new Users.
- Identify any necessary changes to current credit default or User termination rules.
- Identify solutions to any issues derived from the deliberations of the above key points.
- Develop, by consensus, relevant UNC Modification Proposals to deliver any proposed changes to the current arrangements.
- Identify the impact on processes and procedures associated with the implementation of any identified solutions.
- Identify whether any revision to Security arrangements should be made retrospective and what any definition of retrospective should be in this context.

In addition, the Review Group agreed that this consideration of these items be structured around a number of questions to be addressed. These questions are included as an appendix to this document.

The Review Group will provide a written report to the UNC Panel and the final target deliverable shall be to submit any UNC Modification Proposal(s) that has received consensus approval within the Review Group to the UNC Panel by 19 March 2009.

Limits

The Review Group shall focus on changes to the UNC and relevant ancillary/associated documents pertaining to the credit arrangements underpinning User commitments made during Entry Capacity auctions. Where there are other industry arrangements having potential interactions with the outputs from this Review Group, the Review Group may consider the effects that those arrangements may have on this Group's deliberations. For example, the Review Group may wish to consider the outputs from the Transmission Access Review of the electricity transmission regime or developments in the National Grid Gas NTS Offtake Arrangements.

The Review Group will focus on developing UNC Modification Proposals that efficiently address any issues identified in a proportionate and cost effective manner. The Review Group will consider changes required to procedures and processes but will not investigate or develop changes required by IS systems.

Composition

Since the potential impacts of changes to the credit arrangements could be wide-ranging and are as yet uncertain it is essential that the composition of the Review Group covers as many interested parties as possible. Therefore it is desirable that the group is comprised of representatives from National Grid Gas NTS, other Transporters, UNC Users, the Regulator, Storage operators, Interconnector Users, Developers and End Users (and their representative bodies).

The Review Group will comprise the following representation:

Name	Organisation
John Bradley (Chair)	Joint Office of Gas Transporters
Lorna Dupont (Secretary)	Joint Office of Gas Transporters
Ritchard Hewitt (Proposer)	National Grid Gas NTS
Alex Barnes	BG Group
Andrew Fox	National Grid NTS
Benjamin Clair	South Hook Gas
Charles Ruffell	RWE npower
Chris Wright	Centrica
David Linden	BP Gas
Graeme Thorne	Mulberry Capital (for Canatxx)
Jeff Chandler	SSE
Paul O'Donovan	Ofgem
Rekha Patel	Waters Wye Associates
Richard Fairholme	E.ON UK
Robert Cameron-Higgs	Northern Gas Networks
Roddy Monroe	Centrica Services Ltd
Tim Bradley	National Grid NTS

Information Sources

- Uniform Network Code (TPD Sections B, S and V)
- Gas Transporter, Shipper and Supplier Licences
- The Gas Act
- Various industry legislation as appropriate.

Timetable

It is proposed that a total period of 6 months be allowed to conclude this review.

Although the frequency of meetings will be subject to review and potential change by the Review Group it is suggested that the initial frequency of the meetings be every two weeks.

Meetings will be administered by the Joint Office of Gas Transporters and conducted in accordance with the Chairman's Guidelines.

It is anticipated that the timescales over which the review will run will enable any consequential UNC Modification Proposals to be raised and implemented prior to the autumn of 2009.

Appendix: Questions to be Addressed by the Review Group

1. Do the current Default/Termination rules operate effectively and equitably and incentivise appropriate behaviour at the company group level?
2. In the context of the regulatory and licensing regime, under Default/Termination conditions is the balance of the risk shared between the transporter, new and existing Users, large and small portfolio players and the wider Community appropriate?
3. What should we be securing against?
 - eg overall project value, revenue driver value or capacity auction bid value.
4. How far in advance of the capacity release obligation should security be required?
 - What level of security should be provided during this period and, for example, should it be flat or stepped across period?
5. What level of security is needed post capacity release obligation?
 - Flat, tapered etc?
6. Which Security tools are acceptable and should the same tools be available to all Users (New/Existing)?
 - If not, who should be arbiter of what tools are available to each party?
7. Should any revision to Security arrangements be made retrospective and what should the definition of retrospective be in this context?
8. What relevant arrangements are or are proposed in related industries eg CUSC CAP131 in electricity, that might be of assistance?