

Modification Report
Revisions to the Management of Cash Call Accounts (User in Default)
Modification Reference Number 0665

Version 1.0

This Modification Report is made pursuant to Rule 7.3 of the Modification Rules and follows the format required under Rule 8.9.3.

1. The Modification Proposal

It is proposed that Section X of the Network Code is modified as follows:

Where a User is in Administration or Receivership and / or is in Default, as defined by Section V4.3 of the Network Code;

- the User would not be permitted to request the return of monies held in their Cash Call Account until such time that all billing for the period prior to such appointment is completed. (Modify Section X 2.8.7).
- Transco would be allowed to withhold payment of any Energy Balancing Invoice credit item due to a User until such time as the creditors claim had been agreed. In such circumstances Transco would not be obliged to pay interest on the withheld credit value. (Modify Section X3.2.4)

2. Transco's Opinion

Transco view is that this proposal mitigates some of the risks associated with an insolvent User failure by placing tighter controls on the management of Cash Call Accounts. Following a review of the Network Code and the Energy Balancing Credit Rules ("EBCR"), it was identified that by revising the rules governing the management of Cash Call Accounts, the level of risk faced by Users could be reduced thus limiting the risk of financial loss to the shipper community from the operation of the Energy Balancing regime. The principle of the proposal has been discussed with the Energy Balancing Credit Committee, and in accordance with its recommendation, Transco has raised this proposal.

If the existing provisions for the management of Users' Cash Call Accounts were maintained, and a User became insolvent, remaining Users may be faced with higher smearing charges than would be the case if Transco had retained the funds and used these against outstanding credit exposures.

3. Extent to which the proposed modification would better facilitate the relevant objectives

Tighter management of Cash Call Accounts for Defaulting and Insolvent Users would reduce the risk for all Users and, therefore, could be expected to facilitate a more secure and competitive environment in which to operate.

4. The implications for Transco of implementing the Modification Proposal , including

a) implications for the operation of the System:

Transco is not aware of any impact to the operation of the system.

b) development and capital cost and operating cost implications:

Transco is not aware of any development or capital costs from the implementation of the Modification Proposal.

c) extent to which it is appropriate for Transco to recover the costs, and proposal for the most appropriate way for Transco to recover the costs:

Implementation would not cause Transco to incur any additional costs.

d) analysis of the consequences (if any) this proposal would have on price regulation:

Transco is unaware of any such consequence.

5. The consequence of implementing the Modification Proposal on the level of contractual risk to Transco under the Network Code as modified by the Modification Proposal

Transco does not believe that implementing this Modification Proposal would have any consequence on the level of contractual risk to Transco under the Network Code.

6. The development implications and other implications for computer systems of Transco and related computer systems of Users

Transco is not aware of any implications for computer systems.

7. The implications of implementing the Modification Proposal for Users

Transco is not aware of any implications on Users by implementation of this Modification Proposal.

8. The implications of implementing the Modification Proposal for Terminal Operators, Consumers, Connected System Operators, Suppliers, producers and, any Non-Network Code Party

No such implications have been identified.

9. Consequences on the legislative and regulatory obligations and contractual relationships of Transco and each User and Non-Network Code Party of implementing the Modification Proposal

No such implications have been identified.

10. Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantages:

- The tighter management of Cash Call Accounts will protect all Users from any potential financial risk on the shipper community where a User is in Default or Insolvent.

Disadvantages:

- A User in Default or Insolvent would not be able to request monies from its Cash Call Account or receive any credit interest payments, and Transco would insist that the Insolvency Practitioner agrees credit claims before releasing any residual funds.

11. Summary of the Representations (to the extent that the import of those representations are not reflected elsewhere in the Modification Report)

Six representations were received with regard to this Modification Proposal. Five were supportive and one offered qualified support.

Edf Energy Plc, Entergy-Koch Trading Europe Ltd, Powergen UK Plc, British Gas Trading & Total Gas And Power Ltd believe that introduction of the measures identified in this Modification Proposal will reduce the exposure faced by other shippers and thus reduce risk. Total states that "... its implementation will limit the industry's exposure should a shipper enter administration or receivership, which is beneficial to the shipper community". Edf states that "for a User that is in administration, receivership or default, allowing Transco to withhold payment of an Energy Balancing Invoice credit item and not permitting the return of monies held in the Users Cash Call account will reduce the levels of risk for all Users. The tightening of the Credit Rules will decrease the chances of the community receiving financial penalties, as well as facilitating a more secure environment in which to operate and a more competitive environment for all Users". Entergy-Koch states that "The proposal introduces improvements to the management of insolvent shippers such that outstanding bills can be assessed and dealt with prior to money being withdrawn from cash-call accounts".

Powergen believe that this Proposal largely reflects arrangements in place in the Balancing & Settlement Code "... in that Elexon will not return any funds until they are confident that all outstanding amounts due have been paid" and it agrees with the sentiment that interest should not be paid where a user is in Administration or Receivership". Powergen however, "feel that it is prudent to make the following additions to the proposal, that accrued interest will be used to meet: any sums due from the party in Administration; any additional costs incurred by Transco in dealing with Administration issues; any other costs that if not paid by the company in Administration would be recovered by the other shippers".

Transco's response: Transco agrees with the respondent. It proposes to hold all monies in the Cash Call Account which will currently attract interest at 0.5% below the Bank of England base rate applied monthly. Monies held in this

account are treated as security and used to offset that User's debts in line with Network Code section X2.8.8.

British Gas Trading supports this Modification Proposal. It assumes that the Proposal extends to the withholding of "...all Energy balancing Credit items including Gas Reconciliation Energy (GRE) amounts in Reconciliation invoices" but notes that the "current legal drafting does not appear to deliver this."

Transco's response: The current legal drafting references "Energy Balancing Invoice". Section X1.1.6 of the Network Code defines "Energy Balancing Invoice" as an Invoice Document in respect of any Energy Balancing Charges or interest thereon.

British Gas believes that "...in some circumstances the credit amount due to the shipper may be far greater than the amount of 'identified risk' from the failure," and in order to mitigate "...would advocate some mechanism to relate the maximum withholding of the credit due to the assessed level of risk to the community and set this as a limitation of the withhold".

Transco's response: Indebtedness is reported on the net invoice position and any payment back will increase the User's exposure and potentially that of the community. Transco's experience in dealing with Terminations has shown that the credits tend not to exceed amounts due when Users are in default and consequently there has always been a debit smear to the community in these situations. Transco would advocate that a review be undertaken following any future failure as designing such a mechanism may prove to be unnecessarily complicated at this stage.

British Gas believes that there is a "need for timely and accurate communication at such time between concerned parties. The facilitation of a commonly agreed position is key to prompt resolution."

Transco concurs with this view.

Scottish and Southern Energy supports the Proposal but "is concerned that the legal text does not entirely reflect the proposal" and that "it is not entirely clear what would happen to money held by Transco. In particular it is not entirely clear when users would be allowed to request or gain access to money held or whether it would be used to offset outstanding invoices". It is "also concerned that whilst arrangements may have been targeted at Insolvent Users" "...they could in fact have an impact on a wider group of Users. We are not clear whether consideration was given to developing arrangements specifically for instances where an Administrator or Receiver has been appointed".

SSE believes that the "proposed changes to section X2.8.6 and X2.8.7 should include the proposal that a request for return of money could be made once billing and payment for the period has been completed. Similarly changes to X3.2.4 should specify under what circumstances money would be refunded i.e. once creditors claims have been agreed".

Transco's response: Transco supports the comments put forward by SSE and has amended the legal text accordingly. The Proposal has been designed to cover all instances as defined in section V4.3.

12. The extent to which the implementation is required to enable Transco to facilitate compliance with safety or other legislation

Transco is unaware of any change in legislative, regulatory obligations or contractual relationship of Transco, and each User or Non-Network Code Party as a consequence of implementing this Modification Proposal.

13. The extent to which the implementation is required having regard to any proposed change in the methodology established under Standard Condition 4(5) or the statement furnished by Transco under Standard Condition 4(1) of the Licence

This proposal is not required to facilitate any such change.

14. Programme of works required as a consequence of implementing the Modification Proposal

The program of works required to implement this modification proposal includes changes to the Energy Balancing Credit Rules which requires approval by EBCC members and is subject to a 2 month minimum notice period unless agreed otherwise.

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

This modification proposal can be implemented with immediate effect following determination by Ofgem subject to the completion of the work as detailed in 14.

16. Recommendation concerning the implementation of the Modification Proposal

Transco recommends that this proposal is implemented.

17. Restrictive Trade Practices Act

If implemented this proposal will constitute an amendment to the Network Code. Accordingly the proposal is subject to the Suspense Clause set out in the attached Annex.

18. Transco's Proposal

This Modification Report contains Transco's proposal to modify the Network Code and Transco now seeks direction from the Gas & Electricity Markets Authority in accordance with this report.

19. Text

SECTION X: NETWORK CODE SUPPLEMENT

Amend paragraph 2.8.6 to read as follows:

Subject to....

- (a)Cash Call Account;
- (b)Cash Call Limit, and
- (c) the User is not a Defaulting User.

Transco will....

Amend paragraph 3.2.4 to read as follows:

Where:

- (a) Transco has given notice to a User under paragraph 3.2.1, and until the Net Invoice Amount under the relevant Energy Balancing Invoice is paid in full; or
- (b) a User is a Defaulting User.

Transco will not pay and (irrespective of the Invoice Due Date) shall be entitled to withhold payment pursuant to any Energy Balancing Invoice in respect of, any amounts payable to the User in respect of Energy Balancing Charges ("**relevant amounts**") (and no interest shall accrue and be payable on any such amounts from the Invoice Due Date until the day on which the payment is made) and Transco shall instead pay the relevant amounts into the User's Cash Call Account.

Signed for and on behalf of Transco.

Signature:

Terry Grove
Delivery Service Manager

Support Services

Date:

Gas and Electricity Markets Authority Response:

In accordance with Condition 9 of the Standard Conditions of the Gas Transporters' Licences dated 21st February 1996 I hereby direct Transco that the above proposal (as contained in Modification Report Reference **0665**, version **1.0** dated **26/01/2004**) be made as a modification to the Network Code.

Signed for and on Behalf of the Gas and Electricity Markets Authority.

Signature:

The Network Code is hereby modified with effect from, in accordance with the proposal as set out in this Modification Report, version **1.0**.

Signature:

Process Manager - Network Code

Transco

Date:

Annex

1. Any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which The Restrictive Trade Practices Act 1976 ("the RTPA"), had it not been repealed, would apply to this Agreement or such arrangement shall not come into effect:
 - (i) if a copy of the Agreement is not provided to the Gas and Electricity Markets Authority ("the Authority") within 28 days of the date on which the Agreement is made; or
 - (ii) if, within 28 days of the provision of the copy, the Authority gives notice in writing, to the party providing it, that he does not approve the Agreement because it does not satisfy the criterion specified in paragraphs 1(6) or 2(3) of the Schedule to The Restrictive Trade Practices (Gas Conveyance and Storage) Order 1996 ("the Order") as appropriate

provided that if the Authority does not so approve the Agreement then Clause 3 shall apply.
2. If the Authority does so approve this Agreement in accordance with the terms of the Order (whether such approval is actual or deemed by effluxion of time) any provision contained in this Agreement or in any arrangement of which this Agreement forms part by virtue of which the RTPA, had it not been repealed, would apply this Agreement or such arrangement shall come into full force and effect on the date of such approval.
3. If the Authority does not approve this Agreement in accordance with the terms of the Order the parties agree to use their best endeavours to discuss with Ofgem any provision (or provisions) contained in this Agreement by virtue of which the RTPA, had it not been repealed, would apply to this Agreement or any arrangement of which this Agreement forms part with a view to modifying such provision (or provisions) as may be necessary to ensure that the Authority would not exercise his right to give notice pursuant to paragraph 1(5)(d)(ii) or 2(2)(b)(ii) of the Order in respect of the Agreement as amended. Such modification having been made, the parties shall provide a copy of the Agreement as modified to the Authority pursuant to Clause 1(i) above for approval in accordance with the terms of the Order.
4. For the purposes of this Clause, "Agreement" includes a variation of or an amendment to an agreement to which any provision of paragraphs 1(1) to (4) in the Schedule to the Order applies.