

DEVELOPMENT WORK GROUP 0103
REMOVAL OF THE COMMUNITY RISK SECURED CREDIT LIMIT
REPORT FOR PANEL

5 March 1997

1.0 Scope of Development Group

Urgent Modification Proposals 0074 and 0085 proposed a reduction in the 'Community Risk' Secured Credit Limit from £250,000 to £100,000. Following representations on these proposals Ofgas considered that it was important that these issues were addressed through the normal modification process. Ofgas wished to allow time for a full discussion of the issues to take place and to give sufficient time for affected Shippers to put in place the required level of security. In addition, Ofgas' view was that the initial Community Risk limit would remain in place until after the first winter. Subsequently this Development Work Group was formed to investigate the current arrangements and recommend any potential revisions to the rules referenced in Section Su 2.2 of the Code.

The Work Group considered the following:

- (a) the existing Secured Credit Limit rules
- (b) the implications of changes to or removal of the Secured Credit Limit

2.0 Work Undertaken

A paper (attached) was produced by Transco and issued to Work Group members in order to stimulate discussion. The following Development Work Group meetings were held:

27th January - Present: Martin Stanway-Mayers (BP), John Nangle (Amerada), Ken Double (BGT), Nick Wye (Agas), Rob Barnett (ENG), Peter Lambert (Ofgas), Sara Higgins (Transco), Paul McKie (Transco), Phil Carter (Transco)

4th February - Present: Martin Stanway-Mayers (BP), John Nangle (Amerada), Nick Wye (Agas), David Aron (Bell Gas), Megan Watson (Ofgas), Sara Higgins (Transco), Paul McKie (Transco), Phil Carter (Transco)

14th February - Present: Martin Stanway-Mayers (BP), John Nangle (Amerada), David Aron (Bell Gas), Ken Double (BGT), Rob Barnett (ENG), Tim Jones (CNG), Peter Lambert (Ofgas), Sara Higgins (Transco), Rebecca Brealey (Transco), Paul McKie (Transco), Phil Carter (Transco)

2.1 Removal of the Secured Credit Limit

Modification Proposals 0074 and 0085 proposed a reduction in the Community Risk Secured Credit Limit from £250,000 to £100,000.

At the first meeting (27/1) the Work Group considered the following issues:

- The Work Group agreed that operating with the Secured Credit Limit at £250,000 places the Community at unnecessary risk. It is not desirable to continue in this manner through the next winter.
- Proposals 0074 and 0085 were intended to provide an interim measure to reduce the risk over the first winter, with the ultimate aim being to remove the limit entirely.
- The Work Group recognised that Shippers had to have a reasonable period in which to arrange the required level of security. Given that the original proposal to reduce the credit limit was raised on 11th September 1996 the Group felt that Shippers had received sufficient notice to make the appropriate arrangements and that further delays were undesirable.
- The Work Group agreed that the Secured Credit Limit should be reduced as soon as possible.

2.2 Single Guarantee with Split Security

At its first meeting (27/1/97) the Work Group considered a suggestion (made by telephone) of using a single form of security, split between Transportation and Energy Balancing.

- Transco stated that Transportation risk was managed by Transco for its own purposes, whereas Energy Balancing risk related to inter-shipper risk and was managed by TransCo for the Community. Combining the two was not acceptable because it could lead to a conflict of interest. It could also result in practical difficulties given that the two systems are managed independently and relate to separate processes. For Parent Company Guarantees this would not be possible as the community agreed a standard format (see Energy Balancing Credit Rules), whereas TransCo is able to negotiate terms with its customers on a confidential basis where managing its own risk.
- The Work Group agreed that this option was only practicable for a joint letter of credit with a legal split between Transportation and Energy Balancing. This would allow action to be taken if either one of the security limits was exceeded.
- Overall, the Work Group felt that this option ran contrary to the underlying principles of the separate management of Energy Balancing and Transportation risk contained within the Network Code and that separate security for Transportation and Energy Balancing was required. It was important for Shippers to be able to provide security sufficient to cover their operations.

2.3 Reduction of Secured Credit Limit to £50,000

At its second meeting (4/2/97) the Work Group considered the option of a maximum Community Risk Secured Credit Limit of £50,000. This was subject to the Shippers wishing to operate with this level of unsecured credit requiring the support of a Moody's credit rating.

- It was suggested that 20% of the Moody's rating taken from Transportation Risk, would set the limit for a Shipper's unsecured Energy Balancing activity, up to a maximum of £50,000. For a shipper wishing to operate under the Community Risk Secured Credit Limit this level would be established as the lower of £50,000 or 20% of the Moody's rating. Where the 20% level was lower than £50,000 and a Shipper required a higher limit, security for the higher requirement would be necessary.
- The Work Group felt that this was a pragmatic solution in that it would significantly reduce the level of community risk, whilst not necessarily imposing on small shippers the cost of providing additional security.
- However, having considered this proposal further, Transco had concerns over both the appropriateness and practical implications (paper attached) and did not deem it to be a suitable way forward. For example, the initial stage of a Moody's assessment does not establish a monetary amount for which a shipper is good for credit but rather a probability of default rating.

2.4 Reduction of Secured Credit Limit to zero with £50,000 option

At its third meeting (14/2/97) the Work Group considered the option of reducing the maximum Community Risk Secured Credit Limit to zero except under the following circumstances:

- Where the User has already chosen to have a special credit rating for the purposes of obtaining a Transportation related credit limit and this rating (Moody's) is 'Caa' or better then the User can opt to have a £50,000 Community Risk Secured Credit Limit.
- This was subject to the Shipper's Energy Balancing operations being within this £50,000 level. Those Shippers whose operations exceed this level would be required to provide adequate security for the whole of their Secured Credit Limit.
- The Work Group felt that this was a pragmatic solution in that it would significantly reduce the level of community risk and recognises the circumstances of existing smaller shippers who currently have a Moody's rating for Transportation and would obviate the increased financial burden to them of providing additional security in such circumstances.

3.0 Recommendations

The Work Group agreed that a Modification Proposal should be submitted to the March meeting of the Modification Panel to implement the following, with effect from 1 October 1997:

- i) Reduce the Community Risk Secured Credit Limit to zero.
- ii) Provide an exception for those Shippers whose Energy Balancing operations are contained within a £50,000 level. Such Shippers would be able to avail themselves of a £50,000 Community Risk Secured Credit Limit provided that they hold a Moody's credit rating of 'Caa' or above. This would ensure that existing small Shippers are not unnecessarily burdened by the requirement to provide additional security.

4.0 Legal Text

Text for two alternative amendments to paragraph 2.2.2 of the Network Code Supplement, Energy Balancing Credit Management is detailed below.

Text A reflects the Development Work Group's proposal and recognises the circumstances of existing small shippers who currently have a Moody's credit rating for Transportation of 'Caa' or better. On consideration Transco has concerns that this proposal discriminates against future small shippers and is in breach of our statutory duty of non-discrimination. In view of this, Text B is non-discriminatory and would permit future small shippers to avail themselves of a £50,000 Community Risk Secured Credit Limit.

Note: for either alternative the Energy Balancing Credit Rules will be revised to reflect the requirement of those Users who choose to operate under the £50,000 to have a credit rating (Moody's) of 'Caa' or better.

4.1 Text A

Amend Paragraph 2.2.2 of the Network Code Supplement to read as follows:

"2.2.2 For each User the "**Secured Credit Limit**" shall be:

- (a) subject to paragraph (b), the amount determined under paragraph 2.2.3;
- (b) if the User so elects by notice to Transco, where and for so long as the User has at 1 March 1997, and thereafter continues to have, a special credit rating of at least the level specified in the Energy Balancing Credit Rules for the purposes of this paragraph (b), the sum of £50,000."

4.2 Text B

Amend Paragraph 2.2.2 of the Network Code Supplement to read as follows:

"2.2.2 For each User the **"Secured Credit Limit"** shall be:

- (a) subject to paragraph (b), the amount determined under paragraph 2.2.3;
- (b) if the User so elects by notice to Transco, where and for so long as the User has a special credit rating of at least the level specified in the Energy Balancing Credit Rules for the purposes of this paragraph (b), the sum of £50,000."

5.0 Next Steps

Transco is seeking views from the Development Work Group members regarding the alternative Network Code amendments detailed in Section 4 and will submit a Supplemental Report to the Modification Panel members prior to the meeting on 20 March 1997.