

Modification Report
Introduction of the right for the Energy Balancing Credit Committee to instruct National Grid NTS as to appropriate Recovery Steps in respect of Energy Balancing debt

Modification Reference Number 0103

Version 2.0

This Modification Report is made pursuant to Rule 7.3 of the Modification Rules and follows the format required under Rule 9.6.

1. The Modification Proposal

The Proposal was as follows:

“Following Energy Balancing Credit Committee (EBCC) members’ detailed review of the circumstances in which Termination Notices could be issued by the EBCC, members believe that the existing provisions set out within the Uniform Network Code (UNC) in respect of Enforcement and recovery steps for Energy Balancing debt are insufficient and have the potential to expose National Grid NTS to a conflict of interests where a Transportation Debt also exists. Members believe that the provisions of UNC section (X3.4.3) should be amended to provide for the EBCC to instruct National Grid NTS as to the most appropriate recovery action to be taken in order to clearly demonstrate that every effort is being made to curtail the community’s exposure to avoidable financial loss in the event of User default.

Uniform Network Code currently sets out the following provisions in respect of enforcement and recovery steps:

UNC Section X 3.4.2 states “National Grid NTS agrees that it will, subject to the further provisions of this paragraph 3.4, take all reasonable steps to recover Energy Balancing Debt from a defaulting User, and to enforce and realise the Security provided by a defaulting User; provided that nothing in Section X shall require National Grid NTS to initiate or continue any Recovery Steps where to do so would in National Grids NTS’s reasonable opinion expose National Grid NTS or any representative of National Grid NTS to any material risk or liability against which National Grid NTS is not adequately protected by virtue of paragraphs 3.4.4 and 3.4.6.”

UNC Section X3.4.3 builds upon these provisions and states “ National Grid NTS will consult with the Energy Balancing Credit Committee and keep such committee reasonably informed as to the Recovery Steps it takes in relation to Energy Balancing Debt, and circumstances in which National Grid NTS does not consider it commercially worthwhile to take or continue to take such Recovery Steps in relation to Transportation Debt; and will and shall be entitled to discontinue taking Recovery Steps (other than any steps necessary for such discontinuance) where the Energy Balancing Credit Committee has authorised it to do so.”

Currently NTS is not required to take Recovery Steps where to do so would expose it to loss which cannot be recovered by X 3.4.4 and 3.4.6 and thus when acting in accordance with X3.4 it has a means of avoiding such exposure. However if NTS is instructed to act then it would have no such protection. This proposal will amend the UNC such that NTS will be protected from any losses sustained which it cannot recover by X3.4.4 and 3.4.6 when acting in accordance with such instructions.

In addition, this proposal will recognise that following instruction from the EBCC to take appropriate Recovery Steps in respect of Energy Balancing debt should not prevent or delay NTS in the recovery of NTS Transportation debt. This also aligns with the Termination principles in V4.3.

This proposal seeks to revise the provisions of Section X3.4.3 requiring National Grid NTS to convene a meeting of the EBCC as soon as is reasonably practicable following the issue of a Termination Notice to a defaulting User. Scope of such meeting should include but not be limited to the following:

- circumstances under which the User has defaulted
- details of the Users financial position (including details of Energy Balancing Debt, the value of any potential Monthly Adjustment Neutrality Amount in accordance with Section X 1.1 and of any securities held)
- details of the Users Shipper and Supply Licenses /arrangements
- recovery options available and the timescales associated with the implementation of such actions.
- details of the Users portfolio
- provide decision and instruction to National Grid NTS as to how to proceed.”

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

Standard Special Condition A.11.1 (a) “*the economic and efficient operation of the pipe-line system to which this licence relates;*”

The Proposer stated that following “review by the EBCC of Section X of the Uniform Network Code and the EBCR, EBCC believes that the measures identified within this Modification Proposal” would further achievement of this objective “by ensuring that robust procedures and best practice measures are in place to minimise the impact on the industry of User failure.”

“By seeking to limit the exposure of the shipping community (and therefore end consumers) to financial loss,” BGT believed that implementation would facilitate achievement of this objective.

Corona whilst endorsing the Proposer’s view also pointed out that implementation would facilitate achievement of this objective *“as it would limit exposure to Users. The level of exposure to each individual User is determined by subsequent smearing formulae which do not necessarily reflect the impact of the default on the User, particularly as the level of exposure cannot be directly managed by the individual User.”*

EDFE also referred to this objective in stating its belief that implementation would *“ensure that best practice and robust procedures are in place, minimising the risk that shippers, and ultimately consumers, are exposed to.”*

NGNTS also considered that implementation would facilitate achievement of this objective as this Proposal *“sought to introduce improved procedures and best practises through which the level of Energy Balancing financial risk, relating to User default, may be minimised.”*

SGN believed that implementation, by introducing robust and transparent procedures would help facilitate the achievement of this objective.

In reference to this objective, SSE supported implementation as it would ensure that *“robust procedures & best practices are in place to minimise the impact on the industry of User failure.”*

Standard Special Condition A.11.1 (b) *“the co-ordinated, efficient and economical operation of (i) the combined pipe-line system, and/or (ii) the pipe-line system of one or more other relevant gas transporters;”*

NGNTS believed that implementation would align its *“Transportation Debt Recovery arrangements with those of other Transporters Transportation Debt recovery. If implemented this Proposal will remove any perceived advantage NG NTS may have above other Transporters, in respect of Debt Recovery.”* NGNTS, therefore, considered that implementation would facilitate the achievement of this objective.

Standard Special Condition A.11.1 (d) *“the securing of effective competition:... (i) between relevant shippers...”*

NGNTS believed that *“reducing the impact of such avoidable financial risk on the community facilitates a regime which is conducive to the promotion of greater competition”*.

SGN stated that, *“the reduced risk to Users should help facilitate competition.”*

Several respondents referred to the beneficial impact implementation would have on the level of risk for Users and this is consistent with the achievement of this objective. These representations are summarised in Section 7 below.

Standard Special Condition A.11.1 (f) *“the promotion of efficiency in the implementation and administration of...the uniform network code.”*

The Proposer referred to EBCC’s belief that *“making revision to the rules governing the management of Energy Balancing Credit Management, the level of risk faced by Users could be reduced. The revisions proposed demonstrate continued development of the objectives of the EBCR, namely to ‘develop and maintain a Framework for limiting the risk of financial loss to the shipper community resulting from the operation of the Energy Balancing regime’”* and concluded from this that implementation would facilitate the achievement of this objective.

It was also NGUKD’s view that implementation would facilitate achievement of this objective.

SGN also believed that implementation, by introducing robust and transparent procedures would help facilitate the achievement of this objective.

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

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

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:

SGN did not “*envisage major costs as a result of implementing this proposal as changes are only procedural*” and no other respondent identified any development, capital cost or operating cost implications.

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 such 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

BGT believed implementation would provide “*NG NTS with neutrality protection where it does take action.*”

EDFE believed implementation “*would remove the potential conflict of interests that this proposal has identified National Grid Gas (NGG) might be exposed to, whilst ensuring that it has adequate protection for any losses sustained that it can not recover through normal processes.*”

NGNTS was satisfied implementation would provide it “*with sufficient protection from any losses sustained, as a result of the Energy Balancing Debt recovery process, which under prevailing UNC rules NG NTS may not have been able to be recover through X3.4.4 and X3.4.6.*” NGNTS also noted that implementation would effectively separate “*Recovery Steps for Transportation and Energy Balancing Debt.*” It therefore supported the view that “*the proposed changes to the Energy Balancing Debt Recovery should not prevent or delay NG NTS, in the recovery of its Transportation Debt.*”

NGUKD believed that implementation would “*help to remove any conflict which may be perceived to exist for National Grid (NTS) where Transportation and Energy Balancing debt exists. The Proposal also seeks to cover National Grid NTS for any losses sustained in pursuing the Energy Balancing debt under the instruction of the EBCC. UKD believes that this is appropriate.*”

In supporting implementation, SGN agreed that “*NTS should be protected from exposure when acting in accordance with instructions relating to Recovery Steps and such action should not prevent or delay recovery of NTS Transportation 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 implications have been identified.

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

BGT characterised the risk that Users face following a shipper business failure as “*higher than ever*” and consequently that it was “*prudent to continue to seek ways of protecting the shipping community from this prevailing risk exposure*” It believed that this Proposal aimed to “*reduce the cost of any shipper business failure by allowing the EBCC to instruct National Grid NTS to take action against the failing party. Such action will help in reducing the overall burden that will fall to other Users.*”

Corona pointed out that not implementing this Proposal “*would continue to expose the community to unrecovered debt which may have been recoverable. In addition, the conflict of interest experienced by NG NTS would be more likely to be perpetuated. The EBCC, as a committee which represents the interests of Users, should be empowered to review energy balancing risk and direct activities which are reasonable and proportionate to the management of that risk. Ultimately, it is incumbent upon Users to limit risks to the community which cannot be directly managed by any individual Party.*” Corona also believed implementation “*would permit more informed and potentially less biased decision making by a body whose principal objective is to serve the interests of the community it represents.*” It believed implementation should be “*considered on the basis of the current levels of risk incumbent upon Users and whether that level of risk can be justified. In our opinion the current levels of financial risk to Users cannot be justified as they can be better managed by the EBCC which, in serving the community, has an interest in minimising that risk.*”

ExxonMobil thought it was “*appropriate that the Energy Balancing Credit Committee (EBCC) should direct NG NTS as to what recovery steps are to be taken to recover Energy Balancing debt. By protecting NG NTS from losses that it cannot recover under Section X 3.4.4 and 3.4.6, we believe that NG will be better able to take, or to continue taking, such measures when instructed to do so by the EBCC. We believe that this will better protect the shipping community from risk of financial loss in the event of a failed network User.*”

STUK believed implementation “*may reduce the level of risk, faced by Users, through requiring NGG NTS to seek instruction from the EBCC on the most appropriate recovery action to be taken in order to curtail the community's exposure, whilst recognising that this should not prevent or delay NTS in the recovery of NTS Transportation debt. We agree with the Proposer that the EBCC is best placed to issue such instruction.*”

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

Corona suggested the following advantages of implementation:

- *“Limits financial exposure to the Community as a result of Energy Balancing risk.*
- *Permits the Industry, via the EBCC, to play a more proactive role in assessing and managing community risk*
- *Removes the potential for vested or conflicted interests acting against the benefit of the wider community.”*

Disadvantages

- none identified

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

Representations were received from the following:

British Gas Trading Limited	BGT	Support
Corona Energy	Corona	Support
EDF Energy plc	EDFE	Support
ExxonMobil Gas Marketing Europe Limited	Exxon Mobil	Support
National Grid NTS	NGNTS	Support
National Grid (UK Distribution)	NGUKD	Support
RWE npower	RWE	Support
Scotia Gas Networks	SGN	Support
Scottish and /Southern Energy	SSE	Support
Statoil (U.K.) Limited	STUK	Support

All ten respondents supported implementation of the Proposal.

Representations were received on the following subject:

Role of EBCC

BGT believed that the EBCC would be the organisation *“best placed to review the facts in respect of a potentially failing shipper, and subsequently make decisions about the best course of action to be followed.”*

Corona stated that *“the EBCC is, and should be, the vehicle by which decisions relating to the recovery of Energy Balancing Debt should be governed. The current rules place NG NTS in a position which requires that in certain circumstances, it alone and without reference to the community, determines the viability of pursuing debt recovery activities, whilst it is not directly exposed to the consequences of such a decision. In addition, due to its own exposure to unrecovered transportation debt, there is the*

potential for NG NTS to experience a conflict of interest, which again reinforces the view that it may not make decisions in the best interests of Users.”

Convening of EBCC Meeting

NGUKD noted that the Proposal had the stated aim of “revising the provisions of X3.4.3 requiring National Grid NTS to convene a meeting of the EBCC as soon as reasonably practicable following the issue of a Termination Notice to a defaulting User.’ The legal text does not appear to explicitly include such a requirement. UKD believes that the wording provided for X3.4.3 is sufficient on the basis that to keep the EBCC informed and to receive direction will practically require a meeting of the EBCC to be convened. In practice UKD also understands that a meeting will already have been convened under X2.9.7.”

SGN also agreed “that NTS should be required to convene a meeting of the Energy Balancing Credit Committee as soon as reasonably practicable following the issue of a Termination Notice to a defaulting User. At that meeting NTS should advise the EBCC of the details and circumstances surrounding the termination, but more importantly, seek instruction from the EBCC on the most appropriate recovery action to be taken in order to curtail the community's exposure to avoidable financial loss.”

Information Provision

NGNTS noted that “the Proposal suggests that upon authorising the issue of a Termination Notice the EBCC will convene a meeting, the scope of which should address, but is not limited to, the bullet points provided in section 1 of the draft Modification Report. We understand that the details of these information provision requirements will be included as part of the EBCR and note, therefore, that such a list will not be incorporated into the proposed UNC text. We agree that it is appropriate for this level of information provision to be included as part of the EBCR and reside outside of the UNC.”

In respect of the proposed provision of such information, RWE expressed concern that it appeared “the EBCC may be given information about the portfolio of the Shipper in difficulty” It believed that “this information should be given at a sufficiently high level so as not advantage any member of the EBCC should a SoLR situation develop.”

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

No programme for works would be required as a consequence of implementing the Modification Proposal.

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

SGN agreed, "*implementation is feasible within the timescales specified within the proposal.*" This was that implementation could be immediate on receipt of direction from Ofgem.

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

At the Modification Panel meeting held on 19 October 2006, of the 10 Voting Members present, capable of casting 10 votes, 10 votes were cast in favour of implementing this Modification Proposal. Therefore the Panel recommend implementation of this Proposal.

18. Transporter's Proposal

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

19. Text

UNIFORM NETWORK CODE - TRANSPORTATION PRINCIPAL DOCUMENT

SECTION X - ENERGY BALANCING CREDIT MANAGEMENT

Amend paragraph 3.4.2 to read as follows:

~~“3.4.2 National Grid NTS agrees that it will, subject to the further provisions of this paragraph 3.4, take all reasonable steps~~ The Energy Balancing Credit Committee shall direct National Grid Gas as to what Recovery Steps (if any) (the “Directed Recovery Steps”) to take to recover Energy Balancing Debt from a defaulting User, and to enforce and realise the Security provided by a defaulting User; provided that nothing in this Section X shall require National Grid NTS to initiate or continue any Recovery Steps where to do so would in National Grid NTS’s reasonable opinion expose National Grid NTS or any representative of National Grid NTS to any material risk or National Grid NTS agrees that it will, subject to the further provisions of this paragraph 3.4, take the Directed Recovery Steps. To the extent that taking such Directed Recovery Steps exposes National Grid NTS or any representative of National Grid NTS to any liability against which National Grid NTS is not adequately protected by virtue of paragraphs 3.4.4 and 3.4.6, any such liability shall (notwithstanding any other provision of the Code) be deemed to be additional Monthly Neutrality Adjustment Amounts in the month in which National Grid NTS makes payment in respect thereof.”

Amend paragraph 3.4.3 to read as follows:

~~“3.4.3 National Grid NTS will consult with~~ keep the Energy Balancing Credit Committee ~~and keep such committee~~ reasonably informed as to the Directed Recovery Steps it takes in relation to Energy Balancing Debt, ~~and circumstances in which National Grid NTS does not consider it commercially worthwhile to take or continue to take such Recovery Steps in relation to Transportation Debt;~~ and will and shall be entitled to discontinue taking Directed Recovery Steps (other than any steps necessary for such discontinuance) where the Energy Balancing Credit Committee has authorised it to do so.”

Joint Office of Gas Transporters

0103: Introduction of the right for the Energy Balancing Credit Committee to instruct National Grid NTS as to appropriate Recovery Steps in respect of Energy Balancing debt

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 :