

Draft Modification Report
RG0252 Proposal 4: Removal of the use of Specially Commissioned Ratings for the
purposes of obtaining an Unsecured Code Credit Limit
Modification Reference Number 0301
Version 3.0

This Modification Report is made pursuant to Rule 9.3.1 of the Modification Rules and follows the format required under Rule 9.4.

1 The Modification Proposal

Background

Review Group 0252 was raised by Wales and West Utilities in April 2009 seeking to review the existing credit arrangements contained within UNC TPD Section V and ensure that these remain fit for purpose and robust. The review group covered a wide range of credit related topics and produced a set of recommendations which included removing the ability of Users to obtain an Unsecured Credit Limit by using a Specially Commissioned Rating.

UNC TPD V3.1.1 (d) defines a Specially Commissioned Rating as being “*a rating commissioned and paid for by a User with either Moody’s Investor’s Service or Standard and Poor’s and which shall be monitored on a daily basis and reassessed on an annual basis.*” This type of report is available to organisations which do not have a public rating and is specifically requested by and paid for by the User. Such specially commissioned or private ratings can be used by new organisations who have no credit history, but are funded in such a manner that the Credit Rating Agency is able to produce a long term outlook based on a snapshot position.

This type of rating is not subject to the same level of ongoing monitoring by the credit rating agencies as a published rating is, and is not upgraded or downgraded in light of ongoing events, with the snapshot rating valid only at the time that it is initially set. Without further assessments being requested by the organisation, this will result in Specially Commissioned Ratings becoming out of date, and therefore unreliable as a stand alone tool for making assessment and awarding unsecured credit.

The use of Unsecured Credit Limits by means approved within UNC are all subject to rigorous monitoring to ensure that no undue risk is passed on the Transporter, and in the event of failure of a User, through to other Users. The Specially Commissioned Rating cannot be subject to the same type of rigour as other tools used to set Unsecured Credit Limits as they are not continually monitored by the credit rating agency and therefore this is inconsistent with the other credit tools contained within UNC section V. This inconsistency poses a risk to other Users that cannot be reasonably mitigated.

It is further worthy of note that a Specially Commissioned Rating can cost up to £100k to obtain and in the proposers opinion this high cost may be a significant reason why the use of this credit tool has not been utilised by any User.

The Proposal

This modification proposal seeks to remove Specially Commissioned Ratings as an acceptable tool for obtaining an Unsecured Credit Limit.

All other credit tools available within UNC TPD Section V, such as independent assessment, Deposit Deed, etc would continue to be available to the User and in the case of a new User the proposer believes that the use of an independent assessment would be a more cost effective method of obtaining an Unsecured Credit Limit.

Suggested Text

TRANSPORTATION PRINCIPAL DOCUMENT

SECTION V

Amend paragraph V.3.1.1.(b) to read as follows:

“V.3.1.1.(b) An ”Approved Credit rating” is a published and monitored long term issuer rating of not less than Ba3 by Moody’s Investor’s Service or equivalent rating by Standards and Poor’s.”

Delete paragraph V.3.1.1.(d).

Paragraph V.3.1.1 delete the following highlighted/underlined wording:

“ The User shall notify the Transporter within 11 Business Day if the User’s Approved Credit Rating changes or if the User has a reasonable belief that its Approved Credit Rating is likely to change. **Where the User commissions more than one Specially Commissioned Rating it shall notify the Transporter of each such rating and the Transporter shall use the lowest as the Approved Credit Rating**”

Amend paragraph V 3.2.4.(c) to read as follows:

“V.3.2.4.(c) where any published Rating of the User or any person providing security for the User is revised downwards”

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User Pays

a) Classification of the Proposal as User Pays or not and justification for classification

User Pays arrangements are not applicable.

b) Identification of Users, proposed split of the recovery between Gas Transporters and Users for User Pays costs and justification

No User Pays charges applicable.

c) Proposed charge(s) for application of Users Pays charges to Shippers

No User Pays charges applicable to Shippers.

d) Proposed charge for inclusion in ACS – to be completed upon receipt of cost estimate from xoserve

No charges applicable for inclusion in ACS.

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

Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (b): so far as is consistent with sub-paragraph (a), the coordinated, efficient and economic operation of

(i) the combined pipe-line system, and/ or

(ii) the pipe-line system of one or more other relevant gas transporters;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (c): so far as is consistent with sub-paragraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (d): so far as is consistent with sub-paragraphs (a) to (c) the securing of effective competition:

(i) between relevant shippers;

(ii) between relevant suppliers; and/or

(iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (e): so far as is consistent with sub-paragraphs (a) to (d), the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards... are satisfied as respects the availability of gas to their domestic customers;

Implementation would not be expected to better facilitate this relevant objective.

Standard Special Condition A11.1 (f): so far as is consistent with sub-paragraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;

The Proposer believes that the implementation of this modification will make the operation of the UNC in relation to UNC TPD Section V credit rules more

efficient and reduce risk for Users. (Standard Special Condition A11.1 (f)).

4 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.

5 The implications for Transporters and each Transporter of implementing the Modification Proposal, including:

a) Implications for operation of the System:

There are no implications for operation of the System.

b) Development and capital cost and operating cost implications:

There are no cost implications.

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

Not applicable.

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

Not applicable.

6 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

This modification will reduce the contractual risk, which Transporters may be exposed to in relation to failure of a User and bad debt.

7 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 implications have been identified.

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

Administrative and operational implications (including impact upon manual processes and procedures)

No implications have been identified.

Development and capital cost and operating cost implications

No implications have been identified.

Consequence for the level of contractual risk of Users

This modification will reduce the level of residual risk, which Users may bear as a result of failure of another User.

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

No implications have been identified.

10 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 consequences have been identified.

11 Analysis of any advantages or disadvantages of implementation of the Modification Proposal

Advantages

- Consistent approach for monitoring of credit tools
- Reduces unmitigated risk to all Users in the event of another User failure.

Disadvantages

- None identified.

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

Organisation	Response
British Gas Trading	Comments Offered
E.ON UK	Supports
First:utility	Supports
National Grid Distribution	Supports
National Grid NTS	Supports
Northern Gas Networks	Supports

RWE Npower	Supports
Scotia Gas Networks	Supports
ScottishPower	Supports
SSE	Supports
Wales & West Utilities	Supports

In summary, of the 11 responses received, 10 offered support for implementation and 1 offered comments on the Proposal.

SSE considered Specially Commissioned Ratings not to be subject to the same level of ongoing monitoring by the credit rating agencies as a published rating is, and is not upgraded or downgraded in light of ongoing events, with the snapshot rating valid only at the time that it is initially set. This inconsistency poses a risk to other Users that cannot be reasonably mitigated.

RWE npower advises that there is a discrepancy between the proposed legal text and current text where a change has not been highlighted regarding the number of Business Days by which a User should notify the Transporter of a ratings change in TPD Section V3.1.1. Current text states 1 Business Day however the proposed text states 11. RWE npower seeks confirmation as to whether or not this is a typographical error as RWE npower believes 1 Business Day is appropriate as in the original legal text.

British Gas Trading (BGT) supported the implementation of modification 0107V, which sought to allow a User to utilise a Specially Commissioned Credit Rating as a UNC transportation credit tool. Therefore it finds it difficult to support the removal of such a credit tool. The shortcomings given as reasons for its withdrawal would have existed at the time, and to the same extent and BGT considers it is debatable whether those shortcomings were fully recognised at the time. If they were, it is hard to see how this proposal to remove Specially Commissioned Credit Ratings can further the relevant objectives when the introduction of this credit tool under 0107V was deemed to also further the relevant objectives.

13 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.

14 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.

15 Programme for works required as a consequence of implementing the Modification Proposal

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

16 Proposed implementation timetable (including timetable for any necessary information systems changes and detailing any potentially retrospective impacts)

The Proposal could be implemented with immediate effect following direction from Ofgem.

17 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.

18 Recommendation regarding implementation of this Modification Proposal and the number of votes of the Modification Panel

At the Modification Panel meeting held on 19 August 2010, the Panel determined UNANIMOUSLY to recommend implementation of the Proposal.

The Chair noted that eleven representations had been received, of which ten offered support for implementation and one offered comments on the Proposal. He suggested that clear and effective credit requirements within the UNC provide protection and reassurance for all parties, helping to prevent bad debt escalating to inappropriate levels. Requiring credit provision also provides an appropriate barrier to entry. Hence including appropriate credit arrangements within the UNC is consistent with facilitating effective competition between Shippers. Consequently reviewing and improving the arrangements where appropriate is also consistent with facilitating effective competition.

The Panel Chair summarised that Proposal 0301 seeks to remove Specially Commissioned Ratings as an acceptable tool for obtaining an Unsecured Credit Limit. This would remove one route for securing unsecured credit. Since Specially Commissioned Ratings may be considered more risky than other ratings, this may be regarded as improving the UNC credit provisions and so facilitating effective competition. However, removing an opportunity on which some Users may otherwise rely may also be regarded as a barrier to effective competition.

The GdF Suez Panel member questioned the impact of this proposal coupled with 0305 and questioned whether there was a risk that too many options/tools

might be removed.

The Northern Gas Networks Panel member suggested that obtaining a specially commissioned rating was a particularly expensive option, particularly for new businesses, such that it was not used in practice.

The EDF Energy Panel member noted that the Panel had previously recommended the modification, which implemented this tool and questioned what was now different. The National Grid NTS Panel member suggested that since no parties had used the process, there was no case for leaving the tool in place.

The Ofgem Panel representative questioned how this proposal, and others in the series, would be reconciled with Ofgem's published best practice guidelines. The National Grid NTS Panel member believed that the guidelines suggest best practice should be continually reviewed, and the proposals reflected this process. The Wales & West Utilities Panel member added that a letter had been sent to Ofgem requesting the guidelines be reviewed and amended.

19 Transporter's Proposal

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

20 Text

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TRANSPORTATION PRINCIPAL DOCUMENT
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For and on behalf of the Relevant Gas Transporters:

Tim Davis
Chief Executive, Joint Office of Gas Transporters