

Modification proposal:	<b>Uniform Network Code (UNC) 0147: Administration of Unsecured Credit Afforded on the basis of Payment History and Independent Assessment (UNC 0147)</b>		
Decision:	The Authority <sup>1</sup> directs that this proposal be made <sup>2</sup>		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	07 September 2007	Implementation Date:	To be confirmed by the Joint Office

## Background to the modification proposal

This proposal seeks to refine within the UNC the credit arrangements concerned with the provision of unsecured credit by way of payment history and independent assessments.

On 26 January 2007 Ofgem approved modification UNC0113. This modification introduced the ability for a User to obtain a level of unsecured credit based on its payment record. Under this modification the amount of credit afforded to it would increase on a graduated basis each month up to a maximum of 2% of the Transporter's maximum credit limit over a 60 month period provided the User settled all of its transportation invoices by the due date. Any failure to pay by the due date would return the User to 0% unsecured credit.

UNC0113 also introduced the ability for a User to obtain unsecured credit by an independent credit assessment. The assessment would be made by one of a panel of three appointed credit agencies selected by the Transporter. Such assessment would be reviewed annually at the cost of the Transporter. Either party would also have the option to commission an interim reassessment at the cost of the User.

The proposer considers that reducing a User's unsecured credit to 0%, even for the failure to pay a relatively low value invoice was a too great a risk for the User to bear.

Further the proposer considers that it is not best practice<sup>3</sup> for the User to fund all interim re-assessments irrespective of the party requesting them or for the Transporter to select the agency from the panel of three to carry out any independent assessment.

## The modification proposal

UNC0147 will introduce a threshold provision into the UNC. It will provide that where a User fails to pay in full a Transportation invoice of £250 or less, any unsecured credit afforded on the basis of a good payment record will be reduced by 50% on the first such occasion within a 12 month period. Any subsequent failure to pay any Transportation invoice on time within the same 12 month period will reduce the unsecured credit by 100%.

<sup>1</sup> The terms 'the Authority', 'Ofgem' and 'we' are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

<sup>2</sup> This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

<sup>3</sup> In accordance with [Ofgem's best Practice Credit Cover Guidelines, Feb 2005](#)

The proposer considers this will reduce the risk of a User losing all of its unsecured credit obtained by virtue of a good payment record because it may on an occasion fail to pay a comparatively low value invoice on time.

UNC0147 also provides that where a User has been afforded some unsecured credit by way of an independent assessment, any reassessment required outside the initial assessment and the annual review shall be paid for by the party requesting the reassessment. Further the modification provides that it shall be the User that selects one agency from the panel of three that has been provided by the Transporter to carry out an independent assessment.

The proposer considers these three refinements will facilitate achievement of relevant objective (d)<sup>4</sup> because they will implement consistent credit processes more in accordance with best practice thereby helping to ensure that there is no inappropriate discrimination and no inappropriate barrier to entry helping to secure the facilitation of effective competition between relevant shippers.

### **UNC Panel<sup>5</sup> recommendation**

At the modification Panel meeting on 19 July 2007, seven out of nine voting members present voted in favour of implementing this modification proposal. The Panel recommendation therefore was that this modification proposal should be implemented.

### **The Authority's decision**

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 08 August 2007. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposal which are attached to the FMR<sup>6</sup>. The Authority has concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC<sup>7</sup>; and
2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties<sup>8</sup>.

### **Reasons for the Authority's decision**

We agree that the refinements suggested by this modification would facilitate relevant objective (d) and be a move towards best practice. This modification introduces three distinct changes of which we still have some concern about one. We consider the refinements to the procedures and obligations where a User obtains some unsecured credit by way of an independent assessment will both help to facilitate competition and reduce barriers to entry for shippers wishing to enter the market, thereby better facilitating relevant objective (d).

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<sup>4</sup> As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: [http://epr.ofgem.gov.uk/document\\_fetch.php?documentid=6547](http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547)

<sup>5</sup> The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules

<sup>6</sup> UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at [www.gasgovernance.com](http://www.gasgovernance.com)

<sup>7</sup> As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, see: [http://epr.ofgem.gov.uk/document\\_fetch.php?documentid=6547](http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547)

<sup>8</sup> The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986.

The requirement for the requesting party to pay for any interim reassessments as opposed to the User always paying should mean that such assessments are carried out only when it is reasonable to do so and that the User does not pay for interim assessments that were otherwise unnecessary. Similarly, allowing the User to select one agency from the panel of three that have been selected by the Transporter seems equitable.

We do not agree with a respondents comment that the UNC should contain the criteria against which an independent assessment score is allocated. We consider it appropriate that the task of allocating such scores is delegated to relevant commercial experts such as credit assessment agencies. These agencies are obviously not party to the UNC and to have the criteria under which they are required to undertake their assessment in such a contract would potentially create artificial restrictions on credit assessments that may be inconsistent with current commercial practice.

To the extent that these changes may be considered to extend a cross subsidy, as pointed out by one respondent, we consider it is appropriate that Transporters bear the bulk of the cost of annual assessments and interim assessments that they request. They will benefit from seeing the contents of any report provided by the agency carrying out the independent assessment in terms of gaining assurances that a User is a good or bad risk. We do not agree that allowing a User to choose one agency from a panel of three selected by the Transporter removes any integrity from the process. We can not see how this may increase the risk of the end result not being fully independent since all the agencies on the panel of three would have been selected by the Transporter. We consider this aspect of the proposal is a move towards best practice and better facilitates relevant objective (d).

The aspect of this modification with which we still have some concern is to do with the change to obtain unsecured credit by way of a Users payment history. We agree that the proposed change, where a User who fails to pay an invoice of £250 or less on time would lose 50% of any unsecured credit obtained to date, better facilitate relevant objective (d), when compared against the current baseline. However, we have concerns that the setting of the proposed threshold is inflexible and could be improved.

We noted in UNC0113 that;

*"...the requirement for parties to make timely payments is a critical aspect [of obtaining unsecured credit based on payment record], but it is important to note that this requirement should not override the exercise of sensible commercial practice [discretion]"*.

We consider the change proposed does not allow Transporters to exercise sensible commercial discretion in determining the impact of a missed payment on a User's credit levels. There may be occasions where the missed payment may have a satisfactory explanation so as to merit no loss of credit at all, whatever the amount. There may be other occasions, where the amount, no matter how small, may merit a complete loss of credit. This aspect of the modification however does not allow the exercise of such discretion and to that extent it is very limited to the extent that it better facilitates relevant objective (d). It should be noted that whilst we consider the arrangements should provide for the Transporter to exercise sensible commercial discretion, our expectation would be that such sensible commercial practice would be applied in a broadly similar manner by similar companies acting independently of one-another in the same environment.

We do not agree with the respondent that suggested any reduction in the credit limit is permanent. Indeed we consider the suggested legal text specifically provides that Users credit limits based on payment history may be re-established month on month, provided the User makes timely payments. We consider this to be a beneficial aspect in terms of facilitating relevant objective (d).

### **Decision notice**

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority, hereby directs that modification proposal UNC 0147: Administration of Unsecured Credit Afforded on the basis of Payment History and Independent Assessment be made.



**Mark Feather**  
**Associate Director, Industry Codes and Licensing**  
**Signed on behalf of the Authority and authorised for that purpose.**