

Energy Balancing Credit Committee Minutes
Friday 27 May 2011
via Teleconference

Participants

Joint Office (Non voting)

Bob Fletcher (BF) Chair

Xoserve (Non voting)

Mark Cockayne (MC)

Shippers (Voting)

David Holland (DH)

David Trevallion (DT)

John Costa (JC)

Richard Fairholme (RF)

Richard Street (RS)

Observer

Ofgem (Non voting)

Andrew Pester (AP)

Peter Sherry (PS)

Oliver Rix (OR)

Jamie Black (JB)

Apologies

Jenny Higgins (JH)

Tabish Khan (TK)

Gavin Ferguson (GF)

1. Introduction

BF welcomed the members to the meeting, which was quorate.

2. Security of Supply Significant Code Review

Members approved Ofgem presenting an overview of the SCR.

AP presented an overview of progress made to date on the SCR and the potential impacts on credit arrangements. He advised that consultation on the report is expected to open around June/July with the final report due to be published in October 2011.

MC asked which licenced party is to fund compensation. AP advised that consideration is being given to Shippers in these situations and this would link back to the consumer. AP went on to confirm that the view is to move risk from consumers to the industry and insurance can be to be purchased to cover the risk.

JC asked when the obligations are likely to be in place, will there be a settling in of commercial arrangements prior to enforcement of licence obligations ie a soft landing. AP thought a decision is likely with implementation around 2012, which would preclude a soft landing. PS advised that an impact assessment will be influential and though a decision on implementation will be made though the SCR process rather than at a later date.

JB gave an overview of the logic used to develop the draft compensation regime, which is reflective of the cash out price and the potential impacts on credit. He added that there might be a need to include stage payments.

OR explained the model being developed to model scenarios is based on the UK and Ireland markets, using global LNG prices and potential shock price impacts. Identifying cash out prices driven by demand and how these may be frozen and at what stage in the process. The model includes potential compensation results and firm demand changes.

MC asked if the instance of emergency is likely to increase. OR advised it is too early to say at this time.

RS asked if the model takes into account traders credit limits. OR advised that entities are not modelled, it is based on a system value. It is hoped that parties may provide additional information to support the modelling.

RS felt that at other times of emergency, traders credit is impacted and traders may not enter the market due to the potential risk – this may impact the number of traders available to the market. He suggested the model should take account of trader's views or likely actions.

JB was aware of the issue, but advised that it is difficult to quantify the issue and provide a factor in the model.

PS wanted to understand the factors required to reduce the risk of firm interruption. What should be considered ahead of time to influence parties to reduce the risk of volatility in prices?

RS was concerned that the risk has to be factored into what is known on a long-term basis such as an increase in demand and what are short-term impacts, such as a major player failing. The model needs to reflect how parties behave in practice.

MC advised that parties' behaviours might change as more is known about the risk or failure as it unfolds. He was concerned about moving to more volatile cash out price as this may change normal behaviours. Recent experiences have shown that smaller parties can fund gas purchases but find it difficult to underwrite their risk and provide the required security. From an EBCC point of view, normal practice is a letter of credit or cash.

PS asked why smaller parties have found this difficult, as storage facilities are available to offset risks. RS felt this is a cash flow issue for them; they cannot afford to tie up cash in these circumstances, as the money is required to grow the business.

MC advised that smaller participants tend to have more cash available in the summer when the risk is less. They are more at risk when prices are volatile.

PS asked if it is possible to offer different cash out prices based on the

participant. MC was concerned at the potential cost of system changes and wanted to know how it would possible to treat the market equitably if different prices are offered. He explained how Xoserves systems link with Gemini and the potential impacts on both invoicing systems and exposure monitoring systems.

RS was concerned that the proposed changes to EBC rules are going against the principles adopted in the past, which have been seen as fair and consistent. It may provide the wrong incentives for smaller parties, as they will take on additional risk if they grow.

RS was concerned that vehicles may be set up with low trades and low credit risk. At a time of emergency they could take on trades for other parties with the express intention of failure. MC advised that similar examples had been seen, though not to this level.

3. Minutes and Actions from the Previous Meeting

3.1 Minutes

The minutes of the previous meeting held on 08 April 2011 were accepted.

3.2 Actions

EBC 02/01: MC to advise on River Barle's response following their customer interface meeting later in the year.

Update: Action not discussed. **Carried Forward to August**

EBC 01/04: Provide Ofgem with an annual report on credit risk performance over the previous year.

Update: The report is to be provided once the scope has been agreed with Ofgem. **Carried Forward**

EBC 02/04: Arrange a meeting room for the EBCC meeting on 24 June.

Update: Meeting room has been booked **Complete**

EBC 03/04: Amend the Deposit Deed and Credit Rules following discussion at EBCC and circulate amended copies to members.

Update: The documents are currently being clarified with legal teams and a revised copy to be issued soon. **Carried Forward**

EBC 04/04: Consider an update process to monitor implementation of the deed and advise EBCC members.

Update: A plan is currently in progress and should be available once discussions have been concluded with legal teams and systems have been changed. A communication plan is being drafted and should be circulated to members soon. **Carried Forward**

4. Operational Update

MC provided the following Operational update for April 2011.

4.1 Cash Call Notices

During April there were 3 Cash Call Notices issued and 3 were paid.

Further Security Requests (FSRs)

There were no Further Security Requests (FSRs) issued during April 2011

4.2 Settlement:

The following performance was reported:

| Month | Payment Due Date | Payment Due Date +2 |
|-------------------|------------------|---------------------|
| March 2011 | 100% | 100% |
| April 2011 | 100% | 100% |
| Rolling 12 Months | 99.44% | 100% |

5. Modifications

5.1 Alternative to UNC 0233V - Changes to Outstanding Energy Balancing Indebtedness Calculation

MC advised that the review of legal drafting is continuing and a number of issues have been discussed with National Grid, particularly around the clarification of definitions and what the intention of the modification is. A progress update is to be provided at the next meeting.

6. Significant Code Review Update

JC was concerned that there could be impacts on the EBCC as it is likely to be more difficult to manage the risk of failure. RF was concerned how exposure could be monitored this coming winter should Ofgem maintain its aggressive timescale for implementation by 2012.

MC agreed, it would require significant manual workarounds and substantial changes to the UNC – this would not be possible under the current framework and processes, it is not possible to calculate each companies position on a daily basis and keep EBCC informed of changes.

RS thought it would be desirable if Ofgem provided scenarios around the models adopted so that EBCC could evaluate the risk.

MC felt that the implementation of Modification 0233 is essential due to the potential impacts during an emergency situation.

New Action: EBC 05/01 MC to provide information to Ofgem on potential costs for the provision of letters of credit used to provide cover for Energy Balancing.

7. AOB

7.1 Deed of Deposit

MC advised that clarity is to be included in the EBC rules to ensure that parties are aware that two signatures are required from the company for a letter of credit. These changes can be incorporated during the Deed of Deposit changes or rolled out separately. DT asked what the two signatures offer in practice? MC confirmed that no additional cover is offered, but it meets best practice guidelines and provides evidence of governance within the company applying. EBCC agreed it should be rolled in with the Deed of Deposit amendments.

7.2 Review of Financial Institution Aggregate Limits

MC advised that the credit listing for Credit Agricole have been reduced and this required a scale back against 14 Shipper organisations which have been affected and need replacement or supplementary letters of credit. MC further advised that Moodys had put a number of UK banks on watch for potential credit downgrades in the near future and highlighted that this may affect an additional 14 Shippers.

7.3 Market Operator Discussions

MC advised that the EBCC previously sent a letter to the market operator following a meeting earlier in the year, though as yet no response has been received. In the past, the market operator had found it difficult to respond to different market changes due to the way it operated. However, they have changed the way they operate and should EBCC consider increasing their referral level from 60 to 85% as previously discussed. This is in response to the Deed of Deposit changes likely to be implemented soon.

Members agreed to discuss this point at the next meeting.

RS asked if their position can change quickly, do they pose more of a risk. MC felt that recent changes in the way they operate had changed the risk profile, confirming that they are fully underwritten and they have not been over exposed for some sometime.

7.4 Voluntary Discontinuances

MC notified members of 5 companies that wished to voluntarily discontinue, these were:

Fina Exploration – MC advised there were no outstanding issues and members agreed the voluntary discontinuance should proceed.

Finattech Trading - MC advised there were no outstanding issues and members agreed the voluntary discontinuance should proceed.

Fortis bank - MC advised there were no outstanding issues and members agreed the voluntary discontinuance should proceed.

Susquehana Trading Limited - MC advised there were no outstanding issues and members agreed the voluntary discontinuance should proceed.

Economy Gas Trading - MC advised there were no outstanding issues and members agreed the voluntary discontinuance should proceed.

8. Date of Next Meeting

The next planned EBCC meetings is as follows:

Friday 24 June 2011 commencing at 10.30 at Ofgem

Friday 29 July 2011 commencing at 10.30 by teleconference.

Action Log – Energy Balancing Credit Committee

| Action Ref | Meeting Date(s) | Minute Ref | Action | Owner | Status Update |
|-------------------|------------------------|-------------------|---|--------------|----------------------|
| EBC 02/01 | 25/02/11 | 2.2 | Provide River Barle's response following their customer interface meeting later in the year. | Xoserve (MC) | On hold until August |
| EBC 01/04 | 08/04/11 | 3.3 | Provide Ofgem with an annual report on credit risk performance over the previous year. | Xoserve (MC) | Carried Forward |
| EBC 02/04 | 08/04/11 | 5.0 | Arrange a meeting room for the EBCC meeting on 24 June. | Ofgem (TK) | Completed |
| EBC 03/04 | 08/04/11 | 6.1 | Amend the Deposit Deed and Credit Rules following discussion at EBCC and circulate amended copies to members. | Xoserve (LO) | Carried Forward |
| EBC 04/04 | 08/04/11 | 6.1 | Consider an update process to monitor implementation of the deed and advise EBCC members. | Xoserve (LO) | Carried Forward |
| EBC 05/01 | 27/05/11 | 6.0 | Provide information to Ofgem on potential systems impacts and the letters of credit used in Energy Balancing. | Xoserve (MC) | Pending |