

## **Long Term Entry Capacity User Commitment Supplementary Guidance Document**

This document aims to provide supplementary guidance to the draft Modification Proposal being developed by RG221.

### **Stage 1 - Security requirement calculated using Entry Capacity Risk Assessment Process**

All Users with entry capacity holdings will be required to provide appropriate security based on a risk assessment of the allocated capacity values (ACV).

The following allocated capacity values are within scope:

- Allocated QSEC Auction Bid Values Y+2 to Y+16 (Baseline and Incremental).
- Allocated AMSEC Auction Bid Values [only captured if Year +1 Allocated Capacity Values are used (see below)]

Each User will be responsible for ensuring that their credit position is sufficient to cover their capacity holding. The amount of security required will be based on a 2 step process and this is detailed below.

#### **Allocated Capacity Value (ACV)**

Prior to each auction the User will estimate the (max) value of their successful capacity bids across all auction periods and ASEPs in that auction [this value should include enough headroom to cover changes to their bidding strategy] and add this to the value of their existing capacity holding:

3 options for scaling down the Allocated Capacity Value (ACV) are currently being evaluated (yet to be finalised by the Review Group):

- Option 1 – the ACV for the next full Gas Year (Year +1) plus the peak year in the 8 year NPV test period (Y+4 to Y +11 - inclusive).
- Option 2 – All ACV for years Y+2 to Y+16 reduced to either 30%, 25% or 20% [depending on what value the Review Group want to be secured]
- Option 3 – ACV for Y +3, +4, & +5

The table below gives an indication of the ACVs derived through these options.

<b>Option</b>	<b>Auction Bid Value Used (£M)</b>
<b>Option 1 – YR +1 &amp; Peak YR</b>	319.769
<b>Option 2a – YR +2 to YR +16 (30%)</b>	356.452
<b>Option 2b – YR +2 to YR +16 (25%)</b>	297.043
<b>Option 2c – YR +2 to YR +16 (20%)</b>	237.635
<b>Option 3 – YR +3, +4 &amp; +5</b>	427.931

The value selected will be applied to step 2 - Entry Capacity Risk Assessment.

## Entry Capacity Risk Assessment

The ACV derived in step 1 must follow the specified Entry Capacity Risk Assessment process and rules to determine the exact amount to be secured. A scaling factor will allow the ACV (calculated in step 1) to be reduced to an appropriate level (percentage of overall ACV).

The scaling factor will comprise of 2 risk elements and these are described below.

### User Credit Rating (UCR - 50%)

Users will pay between 25% and 50% of the ACV depending on the quality of their credit rating, as specified by Standard and Poor's or Moody's. Where a User currently uses an Independent Assessment Score or Parent Company Guarantee (PCG) as security, for their Transportation Invoicing then the associated rating will be acceptable. [Currently we do not hold a rating for around 50% of Users].

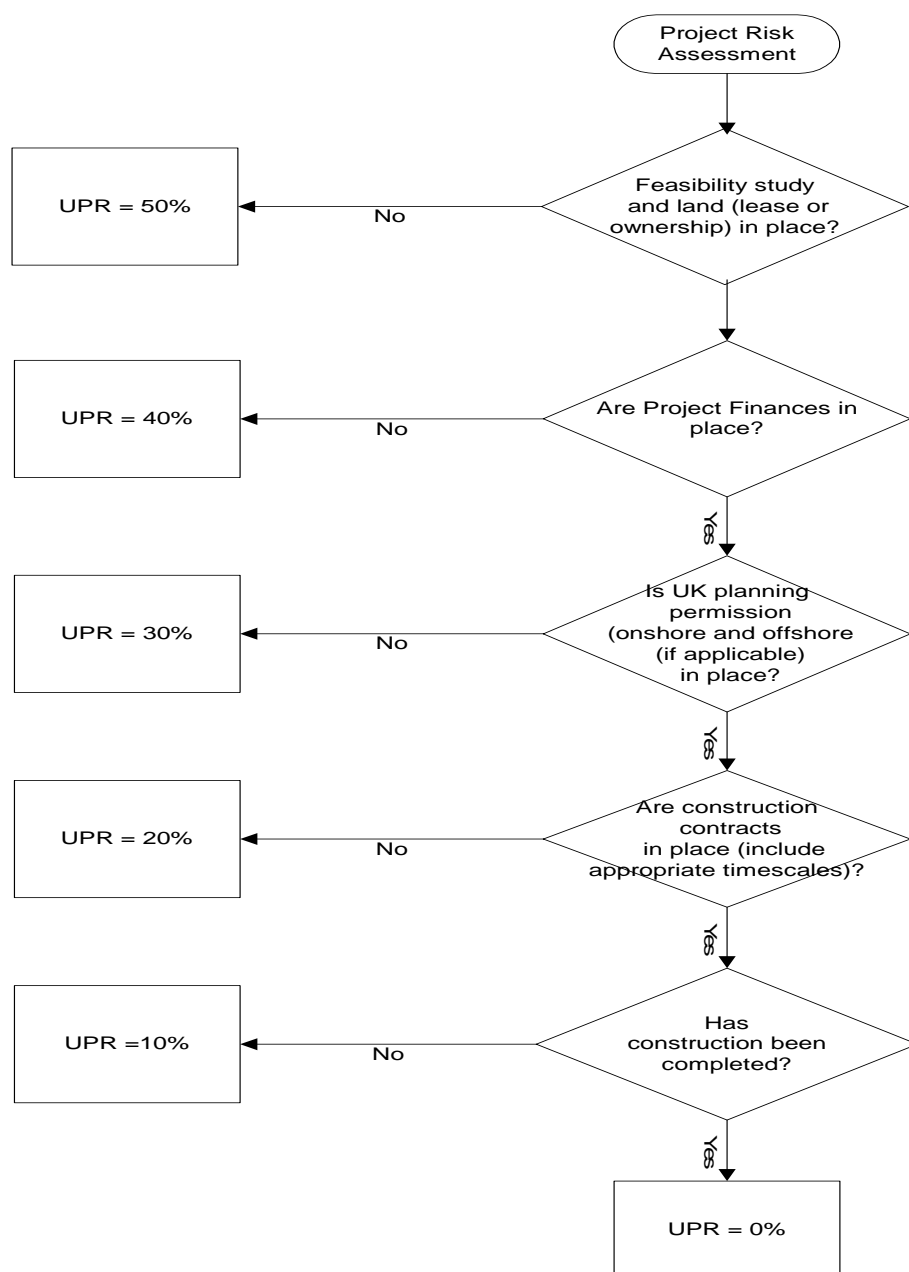
The table below illustrates the UCR risk percentage that applies to the rating specified by Standard and Poor's or Moody's.

<b>Standard and Poor's</b>	<b>Moody's Investors Service</b>	<b>Independent Assessment Score</b>	<b>User Credit Rating (UCR) risk</b>
AAA/AA	Aaa/Aa		25%
A	A		40%
BBB+	Baa1	10	45%
BBB	Baa2	9	45.25%
BBB-	Baa3	8	45.5%
BB+	Ba1	7	45.75%
BB	Ba2	6	46%
BB-	Ba3	5	46.25%
		4	46.625%
		3	47.5%
		2	48.33%
		1	49.125%
No credit rating	No credit rating	0	50%

### User Project Risk (UPR - 50%)

Where a User's entry capacity utilisation is dependent on significant User (UK based) investment to develop an entry facility and or associated pipeline, then a project risk assessment will be undertaken.

If an application is made by a User for Entry Capacity and National Grid is of the opinion that significant User construction Works will be required, then the ACV will be subject to the following Project Risk assessment.



The project activities indicated are such activities that National Grid believes are necessary to ensure that the Entry Capacity allocated is capable of being utilised.

The User must provide the required evidence to support the position of their project; as such information is not in possession, or control, of National Grid. The evidence provided must be sufficient to enable National Grid to be reasonably satisfied that the User has progressed to the next stage. Where the User does not provide National Grid with the required Information then the project will remain at the current stage of assessment and the level of security will remain unchanged.

Where NG is of the reasonable opinion that the status of a project may have changed since the user last demonstrated the position (i.e. a planning appeal has over-turned existing planning permission) then NG will be able to require the User to restate the position of the project within 10 working days. Where there is a dispute between the User and National Grid as to the position of a project in relation to the above flow chart then the National Grid view shall stand but the User may appeal to the Authority.

#### User Security Value (USV)

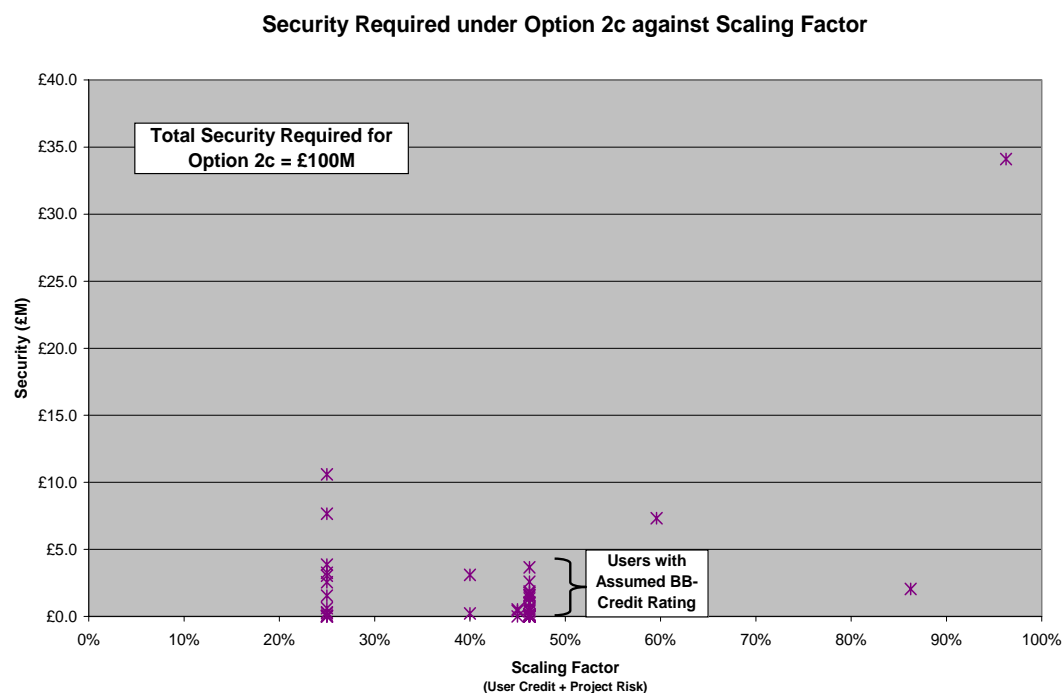
$$\text{User Security Value (USV)} = \text{ACV} * (\text{UCR} + \text{UPR})$$

[Once an option is agreed we can insert a worked example]

The Review Group members have expressed a view that the levels of security to be provided by all Users across all AMSEC and QSEC periods in aggregate should be in the region of £100m-£180m (7-13% of all Allocated Capacity Values). The table below gives an indication of the ACVs used, the security required and the estimated shipper annual operating cost, for the options being considered.

Option	Auction Bid Value Used (£M)	Security Required (USV) (£M)	Security as percentage of total auction bid value (£1.3bn)	Shipper Operating cost (2.5% cost of LOC) per year (£M)
Option 1 – YR +1 & Peak YR	319.769	110.516	8.3%	2.763
Option 2a – YR +2 to YR +16 (30%)	356.452	151.458	11.3%	3.786
Option 2b – YR +2 to YR +16 (25%)	297.043	126.215	9.5%	3.155
Option 2c – YR +2 to YR +16 (20%)	237.635	100.972	7.6%	2.524
Option 3 – YR +3, +4 & +5	427.931	179.245	13.4%	4.481

The graph below gives an indication (for option 2c in table above) of the overall amount of security a User may be required to put in place and the overall risk percentage applied to them.



## **Stage 2 - Security provided to enable participation in the auction**

All Users must ensure that they have sufficient security in place prior to the next auction (QSEC or AMSEC (TBC)) and the required level of security should be the amount calculated in stage 1.

Section V3.4.5 defines the types of security applicable under the Code. For the purposes of long term entry capacity, only the following types of security shall apply:

- "Deposit Deed"
- "Letter of Credit"

Security needs to be provided prior to the QSEC auction window opening. On receipt of security all relevant systems will be updated to allow the User to participate in the Auction.

If the security provided prior to the auction is below the actual amount required (existing holding value plus potential new auction allocation), then NG will prevent all of a User's bids at all entry points across all auction years in that auction from being allocated.

A User will be able to top up their security during the auction bid window (at any point), if they believe that there is or may be a shortfall in their position.

## **Stage 3 – Long Term Entry Capacity Default Rules**

Long term entry capacity "events of default" will be:

- Security is below the required amount (due to a change in Credit Rating risk or Project Risk)
- The security tool (LOC/Bank Deed) is about to expire (less than [28] days).
- The User is terminated in accordance with UNC Section V4 [for other reasons than a LTEC default – the need to link this process to the LTEC default rules is under investigation]

If an "Event of Default" occurs, National Grid will conduct the following process;

- A User will be notified and given 10 business days to put in place sufficient security to cover their capacity holdings
- If the default is not rectified within 10 days:
  - The User will be obliged to pay the amount secured [an invoice may need to be raised for the secured amount or the full auction bid value/commitment - TBC] and National Grid will call on the security provided by the User pending payment of the above invoice.
  - The User will lose the right to participate in any future long term auctions (AMSEC or QSEC) until the above invoice is paid in full.
  - If the invoice is paid, any security previously obtained will be returned to the User. The User will need to provide appropriate security for any additional capacity allocated as part of a future long term auction.
- If the User does not pay the amount specified within the final written demand from NG:
  - National Grid will re-call the User's capacity at all entry points across all years.
  - Where capacity has been previously "Transferred" to another User, National Grid will re-offer the Capacity to them within 5 Business Days, at the original price paid by the first User (in accordance with UNC Section B5.4)
  - Where the other User does not take up the capacity and or spare capacity remains, National Grid will offer the capacity at the next available suitable auction including running an adhoc QSEC or AMSEC auction (at the ASEP/s affected) at NG's discretion.
  - The level of any new Allocated Capacity Values from the resale or B5.4 process will be combined and compared to the original value of the recalled capacity. If there is a short fall in expected revenue then the security provided by the Defaulting User will be used to offset it. Any excess security from the assessment will be returned to the affected User. Any remaining debt will be treated as any other Transportation debt.