

CODE MODIFICATION PROPOSAL No 0305
RG0252 Proposal 8: Unsecured Credit Limit allocated through payment history
Version 1.0

Date: 25/05/2010

Proposed Implementation Date:

Urgency: Non Urgent

1 The Modification Proposal

a) Nature and Purpose of this Proposal

Where capitalised words and phrases are used within this Modification Proposal, those words and phrases shall usually have the meaning given within the Uniform Network Code (unless they are otherwise defined in this Modification Proposal). Key UNC defined terms used in this Modification Proposal are highlighted by an asterisk (*) when first used.

This Modification Proposal*, as with all Modification Proposals, should be read in conjunction with the prevailing Uniform Network Code* (UNC).

Executive Summary

This Modification Proposal seeks to amend the criteria for credit provided by payment history in UNC Transportation Principle Document (TPD) Section V paragraphs 3.1.5 and 3.1.6 to reflect the recommendations of Review Group* 0252 'Review of Network Operator Credit Arrangements' (RG0252) .

It is proposed that credit provision based on a User's payment history is only available as an option for new entrants (upto the 2 year anniversary date of the User acceding to the UNC). It is also proposed that the UNC adopt a revised approach to administration errors that may allow the credit provision to be maintained where a late payment has occurred.

Background

Review Group 0252 was established in July 2009 to undertake a review of the existing credit arrangements within UNC TPD Section V taking into account other credit related issues that have occurred since the publication of the Ofgem Best Practice Guidelines (BPG) document.

One of the topics discussed by the Review Group was Unsecured Credit Limit* risk and in particular the use of independent assessments and payment history in determining the Unsecured Credit Limit to be provided to small Users*. One concern raised by Review Group attendees was that good payment history under the UNC was not always a useful means of gauging if an applicant was fully credit worthy, as they may not be paying other creditors and this would not be visible to the gas transporters.

The current UNC payment history requirements are detailed in TPD Sections V paragraphs 3.1.5 and 3.1.6, briefly these arrangements allow for

payment history to be built up over a 5 year period, however when a payment of greater than £250 is late then any accumulated history would be reset to zero.

The use of payment history as a credit tool to date has been a limited event as Users have opted for other credit tools, such as Letter of Credit* (LoC), Deposit Deed* and independent assessment.

It should be noted that an independent assessment also contains an element of payment history; however this is a more rounded approach that includes a wider payment history check taking into consideration payments to the Transporter(s)* and other parties, when determining the final score/amount of Unsecured Credit Limit to be provided.

RG0252 discussed several potential options for changing the way payment history is currently accrued and, given the aforementioned cross over with independent assessment, the initial preference was to remove payment history as a credit tool. However, following consideration of the views of some small Users about the potential impact on competition it was recognised that new entrants may have difficulty obtaining a full independent assessment until they have been trading for a period of time.

Consideration was also given to reducing the amount of payment history that can be accrued from 5 years to 2 years to limit the exposure to the community. However, the Review Group felt that a further step should also be applied, where a User should move to other credit tools once the initial period of two years expired. This view was provided on the basis that after 2 years the User would have built up sufficient credit history to enable them to undertake an independent assessment.

With the above discussions in mind the Review Group recommended that payment history be retained as a credit tool but that its use be limited to new entrants only with a time limit of a maximum of 2 years from the point they accede to the UNC. After such time the User would need to choose an alternative credit tool and, given that the Review Group have also proposed some enhancements to the independent assessment, this mechanism may be the tool of choice. The Review Group believed this approach would provide responsible credit and limit the exposure to the community of a credit default.

The Review Group also compared the gas payment history processes to the electricity regime (Connection Use of System Code (CUSC)) and it was proposed that the UNC adopt a similar approach to late payments to allow for administration errors. In the current gas regime, if a payment of greater than £250 is late then the accumulated payment history would be reset to zero. In the CUSC a softer landing is applied, where if a payment is received up to and including 2 days after the payment due date then the credit limit would not revert to zero in the first instance.

Nature of the Proposal

It is proposed that TPD Sections V3.1.5 and V3.1.6 should be amended to indicate that credit provision based on a User's payment history is only available as an option up to the 2 year anniversary date of the User acceding to the UNC. After such time the User would not be eligible to use this credit tool. All other credit tools available within TPD Section V, such as independent assessment, Deposit Deed, etc would continue to be available to the User

It is also proposed to amend the aforementioned UNC Sections to allow for User administration errors referred to earlier in this Proposal:

- Amend 3.1.6 to allow for a payment that is received up to and including 2 days after the payment due date. The Unsecured Credit Limit would not increase for the following month and interest would be charged on the late payment.
- However, the Unsecured Credit Limit would not be reset to zero in the first instance but if payment was late more than once within a rolling 12 calendar month period then the credit limit would reset to zero. Interest would also be charged on the second late payment.

This proposal is further illustrated by the following examples:

- Case 1 - User pays on time: User's Unsecured Credit Limit increases (providing all other invoices are paid on the due date in that month) as with the current UNC by 0.033%. The User will only be permitted to increase their Unsecured Credit level for a period of 2 years from the date they accede to the UNC and as a result the maximum level that can be afforded will be 0.8% of 2% of the relevant gas transporter's Regulatory Asset Value* (RAV).
- Case 2 - User misses payment due date on an invoice but pays up to (and inc.) 2 days late: User's Unsecured Credit level remains unchanged and does not increase and interest is charged on the late payment.
- Case 3 – User pays an invoice more than 2 days late: User's Unsecured Credit allowance reverts to zero and interest is charged on the late payment.
- Case 4 – User pays an invoice up to (and inc.) 2 days late on 2 separate occasions within a 12 calendar month rolling period: the Unsecured Credit Limit reverts to zero after the second instance and interest is charged on the late payments.

b) Justification for Urgency and recommendation on the procedure and timetable to be followed (if applicable)

Not applicable

- c) **Recommendation on whether this Proposal should proceed to the review procedures, the Development Phase, the Consultation Phase or be referred to a Workstream for discussion.**

The proposer believes that this Modification Proposal is sufficiently clear to proceed directly to consultation

2 User Pays

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

This Modification Proposal does not affect xoserve systems or procedures and therefore it is not affected by User Pays governance arrangements.

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

Not applicable

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

Not applicable

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

Not applicable

3 Extent to which implementation of this Modification Proposal would better facilitate the achievement (for the purposes of each Transporter's Licence) of the Relevant Objectives

- (d) *so far as is consistent with subparagraphs (a) to (c) the securing of effective competition*

By confining the potential exposure/costs that maybe incurred by gas transporters, shippers and ultimately consumers, as a result of a User credit default this Modification Proposal will reduce a possible barrier to entry and may subsequently increase competition. The proposer believes that limiting payment history to new entrants and restricting its usage to the initial 2 years following accession to the UNC does not prevent such Users from entering the market place.

The Proposal retains all current credit tools for all new entrants during the first 2 years and in addition introduces some allowance for administration errors which takes into account the new User status. Once the User is established i.e. 2 years post acceding to UNC, then the option of credit provision based on payment history would be removed as by this time a User will be able to use the additional credit tools described in UNC Section V.

We believe that this Modification Proposal therefore strikes an appropriate balance

between facilitating new entrants to the market and the risk that such new entrants impose on existing market players and as such furthers this relevant objective.

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

Not applicable

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

a) The implications for operation of the System:

Not applicable

b) The development and capital cost and operating cost implications:

There would be a requirement to make minor changes to the Transporters credit monitoring arrangements.

c) Whether it is appropriate to recover all or any of the costs and, if so, a proposal for the most appropriate way for these costs to be recovered:

Not applicable

d) The consequence (if any) on the level of contractual risk of each Transporter under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal

Reduced contractual risk to gas transporters through limiting both the circumstances/duration that payment history can be used to determine a User's Unsecured Credit Limit and the value that is provided.

6 The extent to which the implementation is required to enable each Transporter to facilitate compliance with a safety notice from the Health and Safety Executive pursuant to Standard Condition A11 (14) (Transporters Only)

Not applicable

7 The development implications and other implications for the UK Link System of the Transporter, related computer systems of each Transporter and related computer systems of Users

Not applicable

8 The implications for Users of implementing the Modification Proposal, including:

a) The administrative and operational implications (including impact upon manual processes and procedures)

- b) **The development and capital cost and operating cost implications**
- c) **The consequence (if any) on the level of contractual risk of Users under the Uniform Network Code of the Individual Network Codes proposed to be modified by this Modification Proposal**

Removing the existing payment history credit tool for Users that have acceded to the UNC for longer than 2 years will reduce the risk of “bad debt” pass through to Users from a credit default.

- 9 **The implications of the implementation for other relevant persons (including, but without limitation, Users, Connected System Operators, Consumers, Terminal Operators, Storage Operators, Suppliers and producers and, to the extent not so otherwise addressed, any Non-Code Party)**

- 10 **Consequences on the legislative and regulatory obligations and contractual relationships of the Transporters**

- 11 **Analysis of any advantages or disadvantages of implementation of the Modification Proposal not otherwise identified in paragraphs 2 to 10 above**

Advantages

- Reduces risk from pass through of bad debt resulting from a credit default.
- Introduces a CUSC style ‘soft landing’ to allow for a User administration error.
- Continues to facilitate new entrants.

Disadvantages

- Removing a form of unsecured credit for a User after 2 years of acceding to UNC.

- 12 **Summary of representations received as a result of consultation by the Proposer (to the extent that the import of those representations are not reflected elsewhere in this Proposal)**

- 13 **Detail of all other representations received and considered by the Proposer**

- 14 **Any other matter the Proposer considers needs to be addressed**

15 Recommendations on the time scale for the implementation of the whole or any part of this Modification Proposal

The Review Group suggest that the Modification Proposal is implemented 3 calendar months after the Authority decision, to allow time for any User affected, to arrange alternative credit tools.

16 Comments on Suggested Text

17 Suggested Text

TPD Section V

Amend paragraph 3.1.5 to read as follows:

“The Transporter may allocate an Unsecured Credit Limit to a User based upon the period of time elapsed that such User has paid all invoices by their due date for payment in accordance with Section S, such that after a calendar month and only until the second anniversary of the User’s User Accession Date, a User may be allocated an Unsecured Credit Limit on the basis of 0.4% of the relevant Transporter’s Maximum Unsecured Credit Limit over a 12 Month period and increasing on an evenly graduated basis each Month up to a maximum of 2 0.8% of the relevant Transporter’s Maximum Credit Limit ~~after 5Years.~~”

Amend paragraph 3.1.6 to read as follows:

“Where a User has been allocated an Unsecured Credit Limit pursuant to paragraph 3.1.5 above, and such User subsequently fails to make payment in full of any invoice (other than in respect of Energy Balancing Charges) issued in accordance with Section S:

~~(a) with a total amount due of £250 or less, then such User’s Unsecured Credit Limit shall be reduced by 50% from the date of such payment default; or~~

(a) on the Invoice Due Date for payment but payment is made in full within 2 Business Days of the Invoice Due Date (“a late payment”), the User shall pay interest on the Invoice Amount and;

(i) where a late payment is made on only one occasion in a 12 Month period the User’s Unsecured Credit Limit shall not be increased in accordance with paragraph 3.1.5 above for that Month;

(ii) where a late payment is made on more than one occasion in a 12 Month period the User’s Unsecured Credit Limit shall be reduced to zero from the date of the second late payment.

~~(b) with a total amount due of greater than £250, or where a User fails to make payment where payment is made more than 2 Business Days from the~~

~~Invoice Due Date on any other occasion within 12 Months of a default as set out in (a) above,~~ then such User's Unsecured Credit Limit shall be reduced to zero from the date of such payment default.

Subject to paragraph 3.1.5 and this paragraph 3.1.6, the User's payment history may continue to be used following the date of any payment default as set out above to increase the reduced value of the User's Unsecured Credit Limit in accordance with paragraph 3.1.5 above.

Code Concerned, sections and paragraphs

Uniform Network Code

Transportation Principal Document

Section(s) V3

Proposer's Representative

Beverley Viney National Grid NTS

Proposer

National Grid NTS