

Modification proposal:	Uniform Network Code (UNC) 0234: “To Correct Drafting Inconsistencies between Sections X and V of the UNC in Respect of User Default and Termination” (UNC 0234)		
Decision:	The Authority ¹ directs that this proposal be made ²		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	27 January 2009	Implementation Date:	To be confirmed by the Joint Office

Background to the modification proposal

Financial responsibilities

Parties that participate in the gas balancing market are responsible for ensuring they are able to meet the financial requirements of balancing the gas they flow into and out of the National Transmission System (NTS) and Local Distribution Zones (LDZ). Users of the gas balancing system are also responsible for the financial risk associated with an individual User being unable to balance their financial position³. The processes used for managing these responsibilities are outlined in the Energy Balancing Credit Rules (EBCR)⁴ and Section X ‘Energy Balancing Credit Management’ and Section V ‘General’, of the Uniform Network Code (the ‘code’)⁵.

Energy balancing credit review

In recent months there have been instances where Users have been in breach of their financial responsibilities under the code, and this has resulted in these Users being terminated⁶. Such Users are defined as being in ‘Default’ and in these circumstances all other Users are held liable for the defaulting Users debt. In light of recent experience, the Energy Balancing Credit Committee⁷ (EBCC) has recently undertaken a review of the EBCR and Section X and V of the code to identify any areas that could be amended to minimise the financial liabilities faced by remaining Users as a result of a User Default.

UNC modification proposal 0234 “To Correct Drafting Inconsistencies between Sections X and V of the code in Respect of User Default and Termination” (the ‘proposal’) is one of three modification proposals developed and put forward as a result of this review⁸.

¹ The terms ‘the Authority’, ‘Ofgem’ and ‘we’ are used interchangeably in this document. Ofgem is the Office of the Gas and Electricity Markets Authority.

² This document is notice of the reasons for this decision as required by Section 38A of the Gas Act 1986.

³ This responsibility is outlined in Section F of the Uniform Network Code (UNC). Further information on the UNC can be found on the Joint Office website at www.gasgovernance.com.

⁴ The EBCR sets out processes and procedures that provide a framework that is used to manage the exposure of all Users to financial loss. The EBCR provides a high level summary of some of the key provisions in the UNC in relation to energy balancing credit. It can be accessed via the Joint Office website at www.gasgovernance.com.

⁵ Section X outlines ‘Energy Balancing Credit Management’ issues under the code and Section V ‘General’ issues under the code.

⁶ When a User is terminated they cease to be a User of the gas balancing system.

⁷ This is a body of industry representatives with certain rights and responsibilities relating to the management of the gas community’s energy balancing credit risk. Further information relating to the activities of the EBCC can be found on the Joint Office website at www.gasgovernance.com.

⁸ The other two modification proposals put forward are UNC 0233 ‘Changes to Outstanding Energy Indebtedness Calculation’ and UNC 0235 ‘Recovery of debt and smearing of revenue via Energy Balancing Neutrality’. These proposals seek to change the UNC to minimise the risk to Users of financial loss resulting

Termination notices⁹

The EBCC review highlighted inconsistencies in Section X and V of the code that relate to the provisions permitting National Grid NTS to issue Termination Notices to defaulting Users. Section X outlines that where Users fail to meet the requests issued to them in an Energy Balancing Management Cash Call¹⁰, a Further Security Request¹¹, an Energy Balancing Invoice¹², and in respect of the appointment of a Receiver¹³ National Grid NTS is permitted to issue a Termination Notice¹⁴. In these circumstances the Termination Notice is effective on the Day following (D+1) the date of the notice.

Section V of the code outlines other circumstances where National Grid NTS is permitted to issue a Termination Notice to a defaulting User. However, unlike in Section X, in these circumstances the Termination Notice is effective from the date specified in the notice. This Section also specifies that if the Termination Notice is issued under Section X it is effective the Day following the date of the notice.

The modification proposal

This proposal seeks to amend Section X and V of the code with regards to when Termination Notices become effective. It seeks to bring Section X in line with Section V by permitting National Grid NTS to make a Termination Notice issued under Section X, effective from the date specified in the notice.

Defining a defaulting User

This proposal also seeks to amend Section V of the code to include all areas of Section X that define circumstances that could lead to a User Default. Section X defines defaulting Users as those that fail to meet the requests issued to them in an Energy Balancing Management Cash Call, a Further Security Request, an Energy Balancing Invoice, and with regard to appointing a receiver.

UNC Panel¹⁵ recommendation

from a User default. Further information relating to these proposals can be found on the Joint Office website at www.gasgovernance.com.

⁹ These notices inform Users of the time and date they will cease to be a User of the gas balancing market. The circumstances in which they are issued are outlined in Section X and V of the UNC. Further information on the UNC can be found on the Joint Office website at www.gasgovernance.com.

¹⁰ An Energy Balancing Management Cash Call is issued when a User exceeds the maximum amount of indebtedness they are permitted to accrue under Section X of the code. Further information can be found in the EBCR on the Joint Office website at www.gasgovernance.com.

¹¹ A Further Security Request is issued to a User when they are issued with two Energy Balancing Management Cash Calls within a particular period. Further information can be found in the EBCR on the Joint Office website at www.gasgovernance.com.

¹² An Energy Balancing Invoice outlines charges a User has incurred as a result of their activities in the gas balancing market.

¹³ A Receiver is a person or company appointed to manage the affairs of a defaulting User. Section V of the code permits National Grid to issue a Termination Notice to a User if their appointed Receiver does not provide adequate assurances to National Grid NTS. For further information please see Section X of the UNC that can be accessed on Joint Office website at www.gasgovernance.com.

¹⁴ The order in which these requests are listed are unrelated to the sequence of notices National Grid NTS issues to Defaulting Users before they are terminated.

¹⁵ The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

At the UNC Panel (the 'Panel') meeting on 18 December 2008 the Panel unanimously recommended implementation of this proposal.

The Authority's decision

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 18 December 2008. 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 FMR¹⁶. The Authority has concluded that:

1. implementation of the modification proposal will better facilitate the achievement of the relevant objectives of the UNC¹⁷; and
2. directing that the modification be made is consistent with the Authority's principal objective and statutory duties¹⁸.

Reasons for the Authority's decision

There were 12 responses to Joint Office's consultation. All 12 responses unanimously supported implementation of the proposal. The views of the Proposer and those expressed by respondents are considered below.

The Authority considers that this proposal will better facilitate relevant objectives (d) and (f) of Condition A11 of the Gas Transporter Licence and is neutral in relation to the remaining objectives. Our reasons for this are provided below.

Relevant objective (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'

Minimising costs

The Authority agrees with the majority of respondents that this proposal could reduce financial loss incurred by remaining Users as the result of a User Default. The proposal provides National Grid NTS with the option to issue a termination notice that is effective on the day specified in the notice rather than at D+1 as is currently permitted by Section X of the code. This option provides National Grid NTS with the ability to minimise the exposure of remaining Users to any additional debt a defaulting User could accumulate. We agree with respondents and the Proposer that this could minimise potential costs to shippers and suppliers and therefore help secure effective competition between these parties.

The Authority notes that this could impinge on a defaulting User's ability to improve their financial position, and thus possibly reduce other Users' exposure to the defaulting debt. However, we are aware that it is common practise for National Grid NTS to discuss the

¹⁶ UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.com

¹⁷ 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

¹⁸The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986.

financial position of a defaulting User with the party concerned and the EBCC, before deciding whether to issue a Termination Notice. As far as is technically and contractually feasible Ofgem would expect this practise to continue in order to provide defaulting Users with adequate notice before they are terminated.

Overall, we consider that this proposal could minimise potential costs to shippers and suppliers, and as such help secure effective competition between these parties.

Promoting competition

We agree with those respondents that considered that this proposal may not necessarily directly enhance competition but could secure effective competition by minimising potential exposure to costs for shippers and suppliers from a User Default. We would expect that any reduction in exposure to costs for shippers and suppliers would help Users to be able to finance their licensed activities on an ongoing basis.

Therefore, we agree with the proposer and the majority of respondents that the proposal better facilitates this objective compared to the current baseline.

Timing

Ofgem notes that it is currently standard practice for National Grid NTS to specify the date as well as the time a Termination Notice will come into effect. As a result of technical processes the time specified is usually the start of the gas day¹⁹. The proposal changes this practice by providing National Grid NTS with the flexibility to specify a time that the notice takes effect which could be before the start of the next gas day. It would also allow National Grid NTS to issue and make effective a Termination Notice within a short period of time, before the next gas day. For example, this proposal would enable a notice issued at 21:00 to be effective before the next gas day, for example at 05:59.

Currently, Sections X and V of the code do not outline current practices with regard to the time a termination notice becomes effective. We note that the proposal does not make provision for a change to current practices (as described in the preceding paragraph) to be reflected in the code. However, the Authority recognises that if parties consider that the code would benefit from further clarification or amendment in this regard they have the ability to raise further modification proposals.

(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 Authority considers that this proposal would improve the consistency with which the code is implemented and administered. We agree with the respondent who considered that the proposal would improve consistency within the code with regard to when Termination Notices are effective and in defining a User Default. We note that the impact of the proposal against this objective is likely to be relatively small, but as a general principle making the code more consistent across relevant Sections is likely to promote efficiency in implementation and administration of the code.

¹⁹ The gas day begins at 06:00 and ends 06:00 the following day. Under the current terms of Section X a Termination Notice would be effective from 06:00 the day following the date specified in the notice.

Overall, we consider that this proposal would better facilitate this objective compared to the current baseline.

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters Licence, the Authority, hereby directs that modification proposal UNC 0234: "To Correct Drafting Inconsistencies between Sections X and V of the UNC in Respect of User Default and Termination" be made.



Ian Marlee
Director, Trading Arrangements

Signed on behalf of the Authority and authorised for that purpose.