Promoting choice and value for all gas and electricity customers

Modification proposal:	**Uniform Network Code (UNC) 0246/246A/246B: Quarterly NTS Entry Capacity User Commitment (UNC246)**		
Decision:	The Authority[1] has decided to reject these proposals		
Target audience:	The Joint Office, Parties to the UNC and other interested parties		
Date of publication:	3 June 2010	Implementation Date:	N/A

Background to the modification proposal

The allocation of long term entry capacity on the gas transmission system is based on the principle of financially backed user commitment. In order to secure capacity at existing entry points or signal to the system operator the need for new capacity, shippers have to bid in Quarterly System Entry Capacity (QSEC) auctions against other shippers. Those shippers that are allocated capacity are then subject to the credit requirements set out in the Uniform Network Code (UNC).

The strength of user commitment is only as good as the robustness of the underlying credit arrangements. Under the existing arrangements, if a shipper defaults on its financial commitments, the shipper's relevant registered QSEC capacity will lapse and they will no longer be considered as holding registered quarterly firm National Transmission System (NTS) entry capacity for that quarterly (three-month) period across all of the Aggregate System Entry Points (ASEPs) where they sought capacity. When the current arrangements were devised, the prospect of a defaulting shipper losing all of its capacity holdings for a quarter was considered to be a proportionate deterrent against the likelihood of credit default. However, this sanction only has genuine effect where a shipper has holdings at multiple ASEPs or where a shipper has multiple obligations at a single ASEP. In the instance where a shipper is delivering against a single obligation from a single ASEP, the cessation of that obligation would allow the shipper to default against the capacity obligation without further penalty. A defaulting shipper still retains its rights to future quarters of capacity secured through the QSEC.

If a shipper defaults on providing security for capacity obtained through the QSEC, National Grid Gas (NGG) can offer any of that entry capacity for resale. However, any under-recovered income would continue to accrue to NGG. As a consequence, the System Operator (SO) or Transmission Owner (TO) commodity charge payable by all shippers increases, to recover the short fall in allowed revenue. In effect, all shippers (and ultimately consumers) are exposed to the financial consequences of the mismatch between the credit underwriting timeframe (ie 12 months prior to capacity flow) and the timeframe over which investment costs accrue (from 42 months prior to capacity flow).

As the patterns of gas delivery to the NTS change, and as the GB market becomes increasingly dependent on overseas gas supplies, significant investment is anticipated to be required to develop import and storage facilities. It is expected that new entrants to the GB gas market who may be single entry point shippers will develop a number of these new projects.

[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.

The prospect that an increasing proportion of the capacity holdings could be held by single ASEP shippers, and that the majority of new infrastructure developments could be instigated by new entrants with no other commitments to the transmission system has raised concerns as to the levels of financial risk to which the shipper community (and ultimately consumers) are exposed.

The modification proposals

Following discussion of the issues in a UNC review group[2], NGG raised UNC modification proposal 246. This attracted two subsequent alternatives 246A and 246B. These proposals focus on how an obligation to put credit in place prior to bidding in a capacity auction might help to prevent industry (and ultimately, consumers) from the effects of default by "risky" projects, but they also propose that defaulting shippers would lose their entitlement to future quarters of capacity secured through the QSEC. The key components of each of these proposals are described in the following sections.

<u>UNC modification proposal 246</u>

UNC modification proposal 246 intends to address the key issues identified by the review group, as follows:

- it proposes that within 28 days of implementation of the proposal, shippers are required to put in place (and subsequently maintain) sufficient security to underpin their existing QSEC holding. The proposal sets the securitisation rate at 10 per cent of the value of the capacity charges due, plus Value Added Tax. Shippers will provide security by either a Deposit Deed or Letter of Credit (LoC) provided by a financial institution with an A rating or above from Moody's, or Standard and Poor's equivalent rating, which cannot be amended or cancelled without agreement of all parties involved.
- 14 days prior to participating in any subsequent QSEC auction, shippers will be required to provide sufficient security to cover both their existing and any anticipated additional capacity holding resulting from their participation in the auction. This means that prior to a QSEC, shippers will be required to estimate their post-auction capacity holdings for the years Y+2 to Y+16, and post credit to cover 10 per cent of the total value of this capacity (plus Value Added Tax at the prevailing rate). This security provision would be in addition to the current provisions that concentrate on QSEC and AMSEC bookings for year Y0 and Y1, ie it adds a new section to the current credit arrangements set out in Section V of the UNC[3].
- in the event of a credit default, it removes the ability for shippers to defer the provision of security which would allow the QSEC provision to lapse. This change also clarifies that the shipper will continue to be treated as holding the relevant NTS entry capacity and will be subsequently invoiced for that capacity. Any failure to pay these invoices will be treated in the same way as any other transportation debt; accordingly, NGG will reject any further QSEC capacity bids at any ASEP submitted by the shipper until the above security has been provided by the shipper.

The proposal gives NGG NTS the ability to reject all capacity bids for a shipper where their existing holding and "anticipated" capacity allocation (plus VAT), would exceed the shipper's prevailing security.

---

[2] Review group 221, "Review of Entry Capacity and the Appropriate Allocation of Financial Risk"
[3] Shippers are required to provide credit for a rolling 12 month average of future capacity bookings

In view of the extra administration required between bidding rounds and the tight timelines around the QSEC, NGG propose that implementation of this proposal would result in fewer bid windows in the QSEC.

The proposal also sets out details of a default process whereby if a shipper default occurs, NGG require the shipper to provide the necessary security cover within the next 10 business days; otherwise the shipper's QSEC capacity holding across all ASEPs in years Y+2 to Y+16 will be recalled and offered in subsequent auctions. The shipper would then be charged a "cancellation fee", equivalent to the value of the security held for the purpose of underwriting the shipper's holding of NTS entry capacity for years Y+2 to Y+16, to cover any shortfall on revenue recovered through subsequent bids for that capacity.

UNC modification proposal 246A

Modification proposal 246A was proposed by EDF Energy. It proposes the same credit cover mechanisms as UNC246, but proposes that the current credit tools detailed within UNC Section TPD V 3.4.6 remain in place. For clarity, these are listed below:

- Bi-lateral insurance
- Deposit deed
- Letter of Credit
- Guarantee

Note that the proposer agreed with NGG that although prepayment agreements are also listed in TPD V 3.4.6, these are not applicable for the securitization of long-term capacity.

UNC modification proposal 246B

UNC246B, submitted by British Gas Trading (BGT), varies from UNC246 in three key aspects:

- it does not require shippers to securitize all existing QSEC capacity holdings. It only requires security for future capacity holdings.
- it allows the full suite of UNC transportation credit tools to remain available.
- it does not use the term "cancellation fee", as BGT believe this terminology legitimises the actions of shippers who renege on previous auction commitments.

A summary of the key points of UNC246 and its alternatives follows.

Table 1: Summary of key features of modification proposals

	UNC246	UNC246A	UNC246B
Prevents deferral of security	√	√	√
Securitizes existing capacity bids	√	√	X
Allows full range of credit tools	X	√	√

UNC Panel[4] recommendation

The UNC Modification Panel met on 21 May 2009 to consider the proposals. Of the nine voting members present, capable of casting ten votes:

- one vote was cast in favour of implementing modification proposal UNC246. Therefore, the Panel did not recommend implementation of proposal UNC246.
- two votes were cast in favour of implementing Alternative Proposal UNC246A. The Panel did not recommend implementation of Alternative Proposal UNC246A.
- nine votes were cast in favour of implementing Alternative Proposal UNC246B. Therefore, the Panel recommended implementation of Alternative Proposal UNC246B.

The Panel then voted on which of the three proposals would be expected to best facilitate achievement of the relevant objectives. One vote was cast in favour of implementing proposal UNC246 in preference to alternative proposals UNC246A and UNC246B. No votes were cast in favour of implementing the alternative proposal UNC246A in preference to proposals UNC246 and UNC246B. Nine votes were cast in favour of implementing the alternative proposal UNC246B in preference to proposals UNC246 and UNC246A.

Therefore, the Panel determined that, of the three proposals, proposal UNC246B would best facilitate the achievement of the relevant objectives.

Ofgem Impact Assessment

Ofgem conducted an impact assessment (IA) on the three proposals, and also included a discussion of alternative means of addressing the perceived consumer credit exposure which were outside the remit of the UNC review group. These related to potential modifications to NGG's gas transporter licence. We received 19 responses to our initial IA. The document and responses can be found on the Ofgem website[5].

Our IA sought to provide estimates of the "break-even default rate" for each proposal. We derived this "break even default rate" though cost-benefit analysis (CBA) which sought to identify the costs of providing security against the minimum average default rate required, so that each proposal would result in a positive benefit. We found the "break-even default rates" for each proposal to be as follows:

- UNC246: 2.6 – 8.2%
- UNC246A: 1.5 – 5.5%
- UNC246B: 0.5 - 2.4%

On this basis, the majority of respondents to the IA considered that UNC246 and UNC246A did not provide value for money and so should not be implemented. Several expressed the view that UNC246B struck a reasonable balance between imposed cost and additional risk for the shipping community, though about three quarters of respondents' first preferences were that none of the proposals should be implemented, as it was considered that the issues could be better addressed through potential changes to NGG's gas transporter licence.

---

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

[5] "User Commitment for National Transmission System Quarterly Entry Capacity - Initial Impact Assessment on modification proposals", Ofgem, Ref 120/09, 7 October 2009

It should be noted that the ranges quoted above are an understatement of the level of default which would be required for the proposals to result in a positive CBA because:

- It was noted by respondents that the key risk against which the industry needed to be protected was the risk that project failure would result in stranded costs, i.e. it should not attempt to cover the risks that established industry parties would go bankrupt. On this basis, if the current approximate 50:50 split remains between new and old capacity, then the effective default rates of the new capacity which carries the stranding risk would need to be double the previously calculated average default rates to result in a positive CBA.
- If the main exposure comes from projects where NGG is required to build capacity, then the profile of revenue at risk would typically follow an "S" curve, ie the main portion of the spend only occurs as the project becomes more certain. If NGG is behaving in an economic and efficient manner, controlling spend to be in line with the related project's development would significantly reduce the likelihood of significant spend on assets that ultimately become stranded.

When factoring in these considerations, it would not be unreasonable to consider the true level of the "break even default rates" to be a factor of four[6] (or more) greater than those illustrated in the IA. This would imply rates of:

- UNC246: 10.4 – 32.6%
- UNC246A: 6.0 – 22%
- UNC246B: 2.0 - 9.6%

The Authority's decision

The Authority has considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 28 April 2010. The Authority has considered and taken into account the responses to the Joint Office's consultation on the modification proposals which are attached to the FMR[7] and responses to the impact assessment carried out by Ofgem.

The Authority has concluded that implementation of modification proposals 246, 246A and 246B will not better facilitate the achievement of the relevant objectives of the UNC as set out in Standard Special Condition A11(1) of the Gas Transporters Licence[8].

Reasons for the Authority's decision

Discussions amongst respondents to the Joint Office of Gas Transporters (JO) consultation in relation to how the proposals might better facilitate the relevant objectives focussed on objectives (a), (c), (d) and (f). We agree that the proposals do not impact on relevant objectives (b) and (e)[9] and so we discuss the impacts on each of objectives (a), (c), (d) and (f) in turn below.

---

[6] Based on the 50:50 split of old:new as described in the first bullet, and that no more than half (and probably significantly less) of the project capex would be spent if there were to be substantive doubts as to the viability of a project. These factors would combine in a multiplicative way to increase the break-even default rates.
[7] UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.com
[8] For Standard Special Condition A11(1) of the Gas Transporters Licence, see: http://epr.ofgem.gov.uk/document_fetch.php?documentid=6547
[9] Standard Special Condition A11.1 (b): so far as is consistent with subparagraph (a), the coordinated, efficient and economic operation of (i) the combined pipe-line system, and/ or (ii) the pipe-line system of one or more other relevant gas transporters;
Standard Special Condition A11.1 (e): so far as is consistent with subparagraphs (a) to (d), the provision of reasonable economic incentives for relevant suppliers to secure that the domestic customer supply security standards… are satisfied as respects the availability of gas to their domestic customers;

Standard Special Condition A11.1 (a): the efficient and economic operation of the pipe-line system to which this licence relates;

We consider that each of UNC246/246A/246B better facilitates this objective, as they prevent shippers from deferring security commitments on booked entry capacity, thereby allowing NGG to make robust decisions based on bookings.

Respondents to the UNC modification process considered that the removal of the ability for shippers to defer security commitments on booked entry capacity (as included in all the proposals) would facilitate achievement of this objective. It was considered that the arrangements would lead to shippers being less willing to engage in speculative behaviour as a failure to provide the requisite security would not just cause a shipper's future capacity holdings to lapse, but that would also mean that they would still be invoiced for that capacity. The removal of such speculative bidding would reduce the risks of either existing capacity being withheld from the market or inefficient investment being triggered, and facilitate the more efficient operation of the NTS.

We agree that shippers should not be able to defer security commitments without any consequence, as this introduces uncertainty about the necessity for the affected capacity and increases the risk that any associated investment will result in stranded assets. This uncertainty has a negative impact on the efficient operation of the network (through hindering its capacity planning activities) and so the removal of this uncertainty would better facilitate the achievement of relevant objective (a).

It should be noted that the primary driver of the uncertainty about the need for additional capacity is the lack of any intermediate stages between the capacity booking process and the release of this capacity; for instance, there is no requirement on the shipper to demonstrate that the project associated with the booked capacity will be operational in line with the capacity release date. The capacity release processes on exit include safeguards such as demonstration dates[10], and this provides both the licensee and shippers with flexibility to overcome problems that might arise with the delivery of facilities, while significantly reducing the likelihood of investing in stranded assets. We would expect the processes around the release of entry capacity to be reviewed as part of the next full Transmission Price Control Review, but absent any necessary licence changes, we consider that the current ability for shippers to defer security commitments on booked entry capacity is detrimental to the efficient operation of the NTS.

Standard Special Condition A11.1 (c): so far as is consistent with subparagraphs (a) and (b), the efficient discharge of the licensee's obligations under this licence;

On balance, we consider that none of the proposals better facilitate this objective. Although all of the proposals act to deter speculative bidding, the costs involved for UNC246 and UNC246A are likely to outweigh the benefits of those proposals. Whereas the costs for UNC246B seem to be more proportionate, we have concerns over whether it is discriminatory.

JO consultation respondents focussed on the point that the current arrangements allow for single ASEP shippers to engage in speculative bidding behaviour without any significant penalty if they subsequently default.

[10] The demonstration date is the final date that users are required to demonstrate to NGG that all relevant consents have been secured and any related construction programme is proceeding to target, if NGG is required to invest in pipeworks or make system reinforcements to provide capacity.

Such bidding behaviour can undermine the strength of auction signals and can also interfere in the bids of other parties, eg it could lead to the triggering of incremental capacity which eventually ends up as a stranded asset. Respondents were largely in agreement that the measures proposed by all of the modification proposals would deter speculative bidding and therefore make the consequential undesirable outcomes less likely.

Ofgem concurs with the views of these respondents on this point. We see the concept of user commitment as integral to NGG's ability to discharge its functions as to the efficient and economic development of the system, so we would tend to favour proposals which reinforce this concept without being unduly burdensome on industry. Our view is that in this regard, all three proposals act to better facilitate the achievement of this objective, as they seek to impose a proportionate deterrent to shippers who would engage in speculative bidding behaviour. This should make the auction signals more reliable for NGG, who can then react to these with a greater degree of certainty.

However, we have concerns with respect to the proposals which we consider to outweigh the above benefit. First, we note that the profile of security cover cost imposed on shippers by all of the proposals does not align with the profile of NGG expenditure. Shippers are being asked to put forward security, and accept potential liabilities, immediately upon being allocated capacity. In instances where new build is required to facilitate the provision of the capacity, NGG's expenditure would be expected to follow an "S" curve (as mentioned previously). This results in a mismatch between the security cover and NGG expenditure, which is in favour of NGG, and is potentially as problematic as the current mismatch of NGG expenditure and shipper liability which has triggered this consideration of credit in the first place. In principle, we would prefer to see systems where the incremental commitment of shippers is aligned with the phased expenditure of NGG.

Further, in the case of UNC246 and UNC246A, we do not believe that the costs being imposed on shippers (and ultimately consumers) are appropriate relative to the risks that are being offset. Our IA and the subsequent responses have highlighted the potentially high rates of default that would be required to justify imposing the proposed costs on shippers. Whereas there is a degree of subjectivity in determining the likelihood of default leading to stranded costs, on the basis of past projects[11] it is unlikely to reach the 22 -33% rates that the higher end of the ranges UNC246/246A would require for a positive CBA. On this basis, we do not consider that these proposals better facilitate this relevant objective.

UNC246B has a significantly lower level of default for achieving a positive CBA, largely because it proposes that current capacity holdings relating to future time periods do not have to be securitised. We were aware of the potentially discriminatory effects this could have, in that if it were to be implemented, shippers could be required to post differing levels of credit for the same type of capacity, depending on when it was booked.

NGG has an obligation to avoid discrimination in the provision of its services. During the development of UNC246, NGG considered it would be necessary to securitize all existing capacity as well as future capacity, as it considered that the application of additional credit requirements to future capacity holders only could be unduly discriminatory.

---

[11] Historically, there have not been any defaults on QSEC capacity holdings, but recently, one incremental capacity project has defaulted, resulting in quarters of the capacity being offered in the Annual Monthly System Entry Capacity auction

In our IA, we discussed the Authority's decision[12] on a related discrimination point with respect to the electricity transmission network and we specifically asked for legally informed views on the potential discrimination point related to UNC246B; none were received. In general, we consider that the level of security cover required against a particular holding should reflect the particular circumstances of the holding and the relevant shipper. In contrast, UNC246B imposes different security cover solely on the basis of a date-related event; the time at which UNC246B is approved. This approach is unlikely to result in a situation where security cover requirements are mapped to the underlying risks of the associated investment. We have not received and are not aware of arguments that would mitigate these concerns and, hence, we have been unable to conclude that the offer of different terms to future capacity holders would not be unduly discriminatory. We have been unable to conclude that UNC246B better facilitates this relevant objective.

Standard Special Condition A11.1 (d): so far as is consistent with subparagraphs (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;

We consider that the UNC246 and UNC246A proposals are neutral in relation to better facilitating competition amongst market participants. In view of the potential discrimination issue outlined above, we have concerns that UNC246B acts against securing effective competition between shippers.

Responses to both consultations were divided on whether any of the modification proposals facilitated the promotion of effective competition. Some incumbents argued that while the need to introduce additional security for capacity holdings would make it more difficult for small players or developers to enter the market, they thought that this was a justifiable barrier in that these categories of shipper were major sources of potential risk. It was considered that any projects that were commercially viable would be able to secure the appropriate backing such that the proposed new credit arrangements would not be a significant impediment. Other respondents highlighted that small developers constitute a major source of innovation in the sector, and that arrangements which act to exclude these players would be of detriment to both the development of competition and longer-term security of supply. These respondents also noted that developers of new entry points are already facing a greater hurdle to entry than those at existing entry points, as new points have to underwrite to the appropriate levels of user commitment before NGG will commit to providing the capacity. They considered that the additional levels of credit proposed by UNC246 and its variants would act as a further barrier to entry for developers of new facilities and skew the arrangements in favour of those with deep pockets, and so be detrimental to competition.

Ofgem notes that a number of respondents stated that projects which are reliant on financing from the banking sector (as distinct from the larger companies who can primarily fund developments from reserves) are normally only able to secure funding once they have acquired the capacity.

[12] The decision letter on CAP131 can be found at http://www.nationalgrid.com/NR/rdonlyres/6ED038C8-9A08-46B3-806B-9C3C330A4F4A/28940/CAP131D.pdf

Their concern is that any requirement for these projects to place security in advance of a QSEC could place these projects under severe financial difficulty. Our view is that projects that are truly financially viable will be able to secure the necessary funding, and that the extra level of scrutiny required demonstrating such viability acts as an additional safeguard. However, we recognise that this might adversely impact on those projects with the most marginal viability, which does act to counter the marginal benefit of having the extra scrutiny in place.

We consider that in view of the potential discrimination point outlined under objective (c) above, we have concerns that UNC246B might have an adverse effect on competition by placing incumbents in a position of long-lasting advantage relative to new shippers. Consequently, we consider that proposals UNC246 and UNC246A have counter-balancing effects on competition, and so are neutral towards the facilitation of this objective, while we are concerned that UNC246B acts against the achievement of this objective.

Standard Special Condition A11.1 (f): so far as is consistent with subparagraphs (a) to (e), the promotion of efficiency in the implementation and administration of the network code and/or the uniform network code;

Ofgem considers that these proposals do not better facilitate this relevant objective. They introduce varying levels of complexity for NGG NTS and shippers, but without benefits that would justify their introduction. On balance, we therefore assess them as being marginally negative against this objective.

Some respondents to the consultations were of the opinion that the proposals created an extra administrative burden through the establishment of new credit requirements for entry capacity and so would not better facilitate this objective. A further respondent claimed that there was some ambiguity as to the intent of proposals UNC246A and UNC246B in relation to whether the amount of credit posted should be reduced in line with a party's credit rating[13] (though this has been clarified by the subsequent provision of legal text for UNC246B).

We agree with respondents that the implementation of any of the proposals would create extra administrative burden for both NGG and shippers. The necessity for shippers to both estimate credit requirements post bidding and then arrange this credit amount in advance of bidding brings additional complexity to a process that is already quite complex; it also places additional burdens on NGG through having to monitor all bids and develop systems to interface with shippers on their credit positions during the auction processes. UNC246 brings extra difficulties through its requirement for the credit to be formed from cash or LoCs, as this is different to the current broader range of tools acceptable for capacity credit. These burdens might be appropriate if they were bringing about significant benefits to the transmission network and its users; however, there is no clear evidence that this is the case. Consequently, we do not consider that any of the variants would better facilitate the achievement of relevant objective (f).

Summary

The consideration above demonstrate that the proposals each have their merits and better facilitate some of the relevant objectives, but act against the achievement of some others.

[13] As per the table in UNC Transportation Principle Document, Section G, 3.1.3 (a)

On that basis, we have come to an overall assessment on each of the proposals, as follows:

UNC246: We consider that this facilitates relevant objective (a) in that it prevents shippers from deferring security commitments on booked entry capacity. However, on balance it does not facilitate relevant objective (c) due to the fact that the proposal imposes an excessive burden of costs on shippers, as reflected in the implied "break-even default rate" required for a positive CBA. It further imposes a cost and liability profile on shippers that is out of step with the associated expenditure by NGG. We believe that it is neutral in relation to securing effective competition (relevant objective (d)) and that it acts against the effective implementation of the UNC (relevant objective (f)) by introducing additional administrative complexity, particularly through the requirement for credit to be formed from cash or LoCs. Accordingly, we do not consider it better facilitates achievement of the relevant objectives.

UNC246A: We consider that this facilitates relevant objective (a) in that it prevents shippers from deferring security commitments on booked entry capacity. However, on balance it does not facilitate relevant objective (c) due to the fact that the proposal imposes an excessive burden of costs on shippers, as reflected in the implied "break-even default rate" required for a positive CBA. It further imposes a cost and liability profile on shippers that is out of step with the associated expenditure by NGG. We believe that it is neutral in relation to securing effective competition (relevant objective (d)) and that it acts against the effective implementation of the UNC (relevant objective (f)) by introducing additional complexity. Accordingly, we do not consider it better facilitates achievement of the relevant objectives.

UNC246B: We consider that this facilitates relevant objective (a) in that it prevents shippers from deferring security commitments on booked entry capacity. However, on balance it does not facilitate relevant objective (c) due to the fact that the proposal is potentially discriminatory. It further imposes a cost and liability profile on shippers that is out of step with the associated expenditure by NGG. We are concerned that UNC246B could hinder effective competition (relevant objective (d)) and consider that it acts against the effective implementation of the UNC (relevant objective (f)) by introducing additional complexity. Accordingly, we do not consider it better facilitates achievement of the relevant objectives.

Next Steps

The proposals were directed at overcoming two specific deficiencies identified by the UNC Review Group 221; namely, the current ability of shippers to retain future capacity holding in the event of a credit default and the perceived additional exposure of industry to risky projects. There was widespread support for the measure to prevent the ability of shippers to defer their security commitments on booked capacity, and as indicated above, Ofgem agrees that the introduction of such a change to the UNC would represent a significant improvement on the current arrangements. The Authority has already approved a similar proposal with respect to exit capacity[14] and without fettering its discretion, would welcome such a proposal with respect to entry capacity. This should allow for a resolution of one of the issues which led to the origination of the modification proposal.

[14] Annual NTS Exit(Flat) Capacity Credit Arrangements (UNC261), approved by Ofgem on 9 December 2009

We are aware of the industry's concerns as to the potential liability arising from a default on incremental capacity. As discussed in our IA, Ofgem's view still remains that it is up to NGG to demonstrate that it has robust credit arrangements in place, and in the absence of such proof, it should not presume that there will be an automatic right to pass on revenue shortfalls arising as a result of a default to the generality of shippers.

Stuart Cook
Senior Partner, Transmission & Governance
Signed on behalf of the Authority and authorised for that purpose.