

## AMENDMENT REPORT

### CUSC Proposed Amendment CAP126

### Clarification of the Applicability and Definition of Qualifying Guarantee and Independent Security

*The purpose of this report is to assist the Authority in their decision of whether to implement Amendment Proposal CAP126*

Amendment Ref	CAP126
Issue	1.0
Date of Issue	15/03/07
Prepared by	National Grid

**I DOCUMENT CONTROL****a National Grid Document Control**

Version	Date	Author	Change Reference
0.1	18/01/07	National Grid	Draft for Industry comment
0.2	15/02/07	National Grid	Draft for Amendments Panel Recommendation Vote
0.3	27/02/07	National Grid	Draft for Amendments Panel Members comment
1.0	15/03/07	National Grid	Formal version for submission to the Authority

**b Document Location**

National Grid Website:

[www.nationalgrid.com/uk/Electricity/Codes/](http://www.nationalgrid.com/uk/Electricity/Codes/)

**c Distribution**

Name	Organisation
The Gas and Electricity Markets Authority	Ofgem
CUSC Parties	Various
Panel Members	Various
National Grid Industry Information Website	

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## 1.0 SUMMARY AND RECOMMENDATIONS

### Executive Summary

- 1.1 Ofgem published a conclusions document on best practice guidelines for gas and electricity network operator credit cover in February 2005. In order to address and codify arrangements relating to the introduction of additional collateral tools CAP099 was implemented in November 2005. Following implementation of CAP099, Ofgem considered that there were particular areas that still needed further development. One of these areas was the use of Parent Company Guarantees and the overlap of Qualifying Guarantees and Independent Security Arrangements.
- 1.2 In order to address this further work, CAP126 Clarification of the Applicability and Definition of Qualifying Guarantee and Independent Security was raised by National Grid. There are currently several issues with the application and definition of Qualifying Guarantees and Independent Security in the CUSC, these are;
- Qualifying Guarantees are treated as a collateral tool and not an allowance. Where a User has a rating that does not afford it an allowance greater than its requirement, the User is using its Parent Company's allowance as an additional collateral tool. The User should instead substitute its allowance with that of its Parent Company.
  - Qualifying Guarantees can be given by a party which is not a parent.
  - A single Qualifying Company can provide many guarantees in excess of its maximum allowance.
  - Independent Security Arrangement can be provided by a parent company as collateral, in addition to the allowance, thus creating 'double counting' in that a user is afforded an unsecured credit limit in excess of its Parent's allowance.

### National Grid Recommendation

- 1.3 National Grid as the proposer of CAP126 is supportive of the Amendment Proposal, believing that it will better facilitate achievement of the Applicable Objectives and should be implemented 10 Business days after an Authority Decision.

### Amendment Panel Recommendation

- 1.4 The Panel voted unanimously that CAP126 DID better facilitate the Applicable CUSC Objectives and was better than the current baseline

## 2.0 PURPOSE AND INTRODUCTION

- 2.1 This Amendment Report has been prepared and issued by National Grid under the rules and procedures specified in the Connection and Use of System Code (CUSC) as designated by the Secretary of State. It addresses issues relating to the clarification of the definition of Qualifying Guarantees and Independent Security.
- 2.2 Further to the submission of Amendment Proposal CAP126 (see Annex 2) and the subsequent wider industry consultation that was undertaken by National Grid, this document is addressed and furnished to the Gas and Electricity Markets Authority (“the Authority”) in order to assist them in their decision whether to implement Amendment Proposal CAP126.
- 2.3 CAP126 was proposed by National Grid and submitted to the CUSC Amendments Panel for consideration at their meeting on 29<sup>th</sup> September 2006 where it was agreed that a Working Group should consider the proposal. CAP126 Working Group Report was submitted to the CUSC panel meeting on 24<sup>th</sup> November 2006. Following evaluation by the Working Group, the Amendments Panel determined that CAP126 was appropriate to proceed to wider industry consultation by National Grid.
- 2.4 This document outlines the nature of the CUSC changes that are proposed. It incorporates National Grid’s recommendations to the Authority concerning the Amendment. Copies of all representations received in response to the consultation have been also been included and a ‘summary’ of the representations received is also provided. Copies of each of the responses to the consultation are included as Annex 3 to this document.
- 2.5 This Amendment Report has been prepared in accordance with the terms of the CUSC. An electronic copy can be found on the National Grid website, at [www.nationalgrid.com/uk/Electricity/Codes/](http://www.nationalgrid.com/uk/Electricity/Codes/).

## 3.0 PROPOSED AMENDMENT

- 3.1 CAP126 proposes to amend the CUSC Section 3, Part III (Credit Requirements) to clarify the definition and applicability of Independent Security and the definition and applicability of Qualifying Guarantees.
- 3.2 Currently within CUSC Section 3, a ‘Qualifying Guarantee’ and ‘Independent Security Arrangement’ are open to misinterpretation by Users.
  - Qualifying Guarantees are currently treated as a collateral tool and not an allowance. Where a User has a rating that does not afford it an allowance greater than its requirement, the User is using its Parent Company’s allowance as an additional collateral tool. The User should instead substitute its allowance with that of its Parent Company.
  - Qualifying Guarantees can currently be given by a party which is not a parent.
  - A single Qualifying Company can currently provide many guarantees in excess of its maximum allowance.
  - Independent Security Arrangement can be provided by a parent company as collateral, in addition to the allowance, thus creating ‘double counting’

in that a User is afforded an unsecured credit limit in excess of its Parent's allowance.

3.3 It is proposed that Qualifying Guarantees are:

- only to be provided from a Parent Company;
- only to be used as an allowance; and
- in aggregate all Parent Company Guarantees cannot exceed the Parent's maximum allowance by reference to Appendix 1 of Section 3, Part III of the CUSC.

3.4 It is proposed that Independent Security is:

- not be issued from a Parent Company to a direct subsidiary;
- only be issued by Parent Companies to non-subidiaries; and
- only be used as a collateral tool

## **4.0 ASSESSMENT AGAINST APPLICABLE CUSC OBJECTIVES**

### **Proposed Amendment**

4.1 CAP126 would better facilitate the CUSC Objective(s);

(a) the efficient discharge by the Licensee of the obligations imposed upon it by the act and the Transmission Licence; and

(b) facilitating effective competition in generation and supply of electricity and facilitating such competition in the sale, distribution and purchase of electricity.

4.2 The increased transparency given by clarifying the applicability and definition of Qualifying Guarantee and Independent Security will better facilitate Objective (a), by increasing efficiency and Objective (b) by increasing competition to enable a User to make a more informed decision on the allowances and collateral tools available to them in order to manage their security requirements.

4.3 Moving Qualifying Company Guarantees from collateral to User's Credit Allowances will remove potential under securitisation caused by double counting and this will better facilitate effective competition (Objective (b)), by ensuring that an appropriate level of security was held for all parties, and by reducing the chances of bad debt being passed through to the industry.

## **5.0 PROPOSED IMPLEMENTATION**

5.1 The Working Group and National Grid propose CAP126 should be implemented 10 Business Days after an Authority decision as it seeks only to clarify the applicability and definitions used within the CUSC and does not change the principle introduced by CAP099, which implemented additional collateral tools.

5.2 No respondents to the CAP126 consultation expressed a view on the proposed implementation date. There is, therefore, no disparity between the view of the Industry and that of National Grid

## **6.0 IMPACT ON THE CUSC**

- 6.1 CAP126 requires amendments to Section 3, Part III- Credit Requirements and Section 11 – Interpretation and Definitions of the CUSC.
- 6.2 The text required to give effect to the Proposal is contained as Annex 1 of this document.

## **7.0 IMPACT ON CUSC PARTIES**

### **Proposed Amendment**

- 7.1 CAP126 in the view of the proposer it is an amendment to provide greater transparency as to the definition and application of collateral tools and has no further impact upon CUSC parties.

## **8.0 IMPACT ON INDUSTRY DOCUMENTS**

### **Impact on Core Industry Documents**

- 8.1 CAP126 has no impact upon Core Industry Documents.

### **Impact on other Industry Documents**

- 8.2 CAP126 has no impact upon other Industry Documents.

## **9.0 IMPACT ON INDUSTRY COMPUTER SYSTEMS OR PROCESSES**

- 9.1 CAP126 has no impact upon on Industry Computer Systems or Processes.

## **10.0 VIEWS AND REPRESENTATIONS**

- 10.1 This Section contains a summary of the views and representations made by consultees during the consultation period in respect of the Proposed Amendment.

### **Views of Panel Members**

- 10.2 No views or representations were made by Panel Members in their capacity as Panel Members during the Consultation.

### **View of Core Industry Document Owners**

- 10.3 No views or representations were made by Core Industry Document Owners.

### **View of Working Group**

- 10.4 The Working Group supports CAP126 and believes it should be implemented and no view or representations were made by Working Group Members in their capacity as Working Group during the Consultation.

## Responses to Consultation

- 10.5 The following table provides an overview of the representations received. Copies of the representations are attached as Annex 3.

Reference	Company	Supportive	Comments
CAP126-CR-01	E.ON UK	YES	E.ON UK supports CAP126 believing it will better facilitate both CUSC Applicable Objectives, (a) and (b) and would bring this area of network operator credit cover in line with Ofgem's best practice guidelines

## 11.0 AMENDMENT PANEL RECOMMENDATION

- 11.1 The CUSC Amendments Panel Recommendation Vote on CAP126 was conducted at the Panel Meeting on 23<sup>rd</sup> February 2006.
- 11.2 In summary the Panel voted CAP126 DID better facilitate the Applicable CUSC Objectives and was better than the current baseline.
- 11.3 The Panel Members present unanimously believed CAP126 better facilitated Applicable Objective (a) and (b).

## 12.0 NATIONAL GRID RECOMMENDATION

- 12.1 National Grid as the proposer of CAP126 is supportive of the Amendment Proposal, believing that it will better facilitate achievement of the Applicable Objectives, by increasing transparency and clarifying the applicability and definition of Qualifying Guarantee and Independent Security. This will increase competition to enable a User to make a more informed decision on the allowances and collateral tools available to them in order to manage their security requirements and by moving Qualifying Company Guarantees from collateral to User's Credit Allowance it will remove potential under securitisation caused by double counting and this will better facilitate effective competition (Objective (b)), by ensuring that an appropriate level of security was held for all parties, and by reducing the chances of bad debt being passed through to the industry.

## 13.0 COMMENTS ON DRAFT AMENDMENT REPORT

- 13.1 National Grid received no responses following the publication of the draft Amendment Report.

**ANNEX 1 – PROPOSED LEGAL TEXT TO MODIFY THE CUSC****Text to give effect to the Proposed Amendment****PART III - CREDIT REQUIREMENTS****3.21 BSUOS CHARGES AND TNUOS DEMAND CHARGES: PROVISION OF SECURITY COVER**

- 3.21.1** Each **User** required to pay **Use of System Charges** shall provide **Security Cover** for **Balancing Services Use of System Charges** and **Transmission Network Use of System Demand Charges** from time to time in accordance with this Part III.
- 3.21.2** Each such **User** shall not later than the date of its accession to the **CUSC Framework Agreement** deliver to **The Company** evidence reasonably satisfactory:-
- (a) to establish the **User's Allowed Credit**; and
  - (b) if required, that it has provided and is not in default under the **Security Cover** referred to in Paragraph 3.21.3 below.
- 3.21.3** The **User** shall be required to provide **Security Cover** where its **Security Requirement** exceeds its **User's Allowed Credit**. If such **User** is required to provide **Security Cover** it shall, not later than the date of:-
- (a) the date of its becoming a party to the **CUSC Framework Agreement**; or
  - (b) two **Business Days** after **NGC** notifies the **User** in writing that the **Security Cover** required exceeds the **Security Amount** provided; or
  - (c) where and to the extent that the amount of **Security Cover** required exceeds the **Security Amount** provided as a result of a **User's** revised forecast given in accordance with Paragraph 3.10 within one month of such revised forecast being provided to **NGC**:-



- ~~(i) deliver to **The Company** a **Qualifying Guarantee** in such amount as shall be notified by **The Company** to the **User** in accordance with Paragraph 3.22; and/or~~
- (ii) deliver to **The Company** a **Letter of Credit** (available for an initial period of not less than 6 months) in such amount as shall be notified by **The Company** to the **User** in accordance with Paragraph 3.22; and/or
- ~~(iii)~~ deliver to **The Company** cash for credit to the **Escrow Account** in such amount as shall be notified by **The Company** in accordance with Paragraph 3.22; and/or
- ~~(ivii)~~ deliver to **The Company** a **Bilateral Insurance Policy** in such an amount as shall be notified by **The Company** to the **User** in accordance with Paragraph 3.22; and/or
- (iv) deliver to **The Company** an **Insurance Performance Bond** in such an amount as shall be notified by **The Company** to the **User** in accordance with Paragraph 3.22; and/or
- (vi) delivery to **The Company** an **Independent Security Arrangement** in such an amount as shall be notified by **The Company** to the **User** in accordance with Paragraph 3.22.

3.21.4 The provisions of this Part III shall be in addition to any other requirements to provide security in respect of any other sums due under the terms of the **CUSC** or any **Bilateral Agreement** or **Construction Agreement**.

3.21.5 Maintenance of Security Cover

Where a **User** is required to provide **Security Cover** in accordance with the terms of this Paragraph 3.21 it shall at all times thereafter maintain a **Security Amount** equal to or more than the **Security Cover** applicable to it. Immediately upon any reduction occurring in the **Security Amount** provided by the **User** or any **Letter of Credit** ~~or **Qualifying Guarantee**~~ or **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** being for any reason drawn down or demanded respectively, the **User** will procure that new **Letters of Credit**, ~~or **Qualifying Guarantees**~~ or **Bilateral Insurance Policies**, ~~or **Insurance Performance Bonds**~~ or **Independent Security Arrangements** are issued or existing **Letters of Credit**, ~~or **Qualifying Guarantees**~~ or **Bilateral Insurance Policies**, ~~or **Insurance Performance Bonds**~~ or **Independent Security Arrangements** are reinstated (to the satisfaction of **The Company**) to their full value or cash is placed to the credit of the **Escrow Account** in an amount required to restore the **Security Amount** to an amount at least equal to the **Security Cover** applicable to the **User**, and in such proportions of **Letters of Credit**, ~~**Qualifying Guarantees**~~ or **Bilateral Insurance Policies**, ~~or **Insurance Performance Bonds**~~ or **Independent Security Arrangements** and/or cash as the **User** may determine. Not later than 10 **Business Days** before any outstanding **Letter of Credit**,

~~and/or Qualifying Guarantee or~~ **Bilateral Insurance Policy**, ~~or~~ **Insurance Performance Bond** ~~and/or Independent Security Arrangement~~ is due to expire, the **User** shall procure to the satisfaction of **The Company** that its required **Security Amount** will be available for a further period of not less than 6 months which may be done in one of the following ways:-

- (a) subject to the issuing bank continuing to have an **Approved Credit Rating** for an amount at least equal to the required **Security Amount** applicable to it (less its balance on the **Escrow Account**) provide **The Company** with confirmation from the issuing bank that the validity of the **Letter of Credit** has been extended for a period of not less than 6 months on the same terms and otherwise for such amount as is required by this Part III; or
- (b) provide **The Company** with a new **Letter of Credit** issued by an issuing bank with an **Approved Credit Rating** for an amount at least equal to the required **Security Amount** applicable to it (less its balance on the **Escrow Account**) which **Letter of Credit** shall be available for a period of not less than 6 months; or
- ~~(c) subject to the entity issuing the **Qualifying Guarantee** continuing to have an **Approved Credit Rating** for an amount at least equal to the required **Security Amount** applicable to it (less its balance on the **Escrow Account**) provide **The Company** with confirmation from the issuing entity that the validity of the **Qualifying Guarantee** has been extended for a period of not less than 6 months on the same terms and otherwise for such amount as is required by this Part III; or~~
- ~~(d) provide **The Company** with a new **Qualifying Guarantee** for an amount at least equal to the required **Security Amount** applicable to it (less its balance on the **Escrow Account**) which **Qualifying Guarantee** shall be available for a period of not less than 6 months; or~~
- (~~e~~) procure such transfer to **The Company** for credit to the **Escrow Account** of an amount as shall ensure that the credit balance applicable to the **User** and standing to the credit of the **Escrow Account** shall be at least equal to the required **Security Amount**; or
- (~~d~~) subject to the entity issuing the **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** continuing to meet the **Requirements** provide **The Company** with confirmation from the issuing entity that the validity of the **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** has been extended for a period of not less than 6 months on the same terms and otherwise for such amount as is required by this Part III; or
- (~~e~~) provide **The Company** with a new **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** for an amount at least equal to the

required **Security Amount** applicable to it (less its balance on the **Escrow Account**) which **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** shall be available for a period of not less than 6 months.

### 3.21.6 Failure to supply or maintain Security Cover

If the **User** fails at any time to provide or maintain **Security Cover** to the satisfaction of **The Company** in accordance with the provisions of this Part III, **The Company** may at any time while such default continues, and if at such time any **Letter of Credit** and/or ~~**Qualifying Guarantee**~~ and/or **Bilateral Insurance Policy** and/or **Insurance Performance Bond** and/or **Independent Security Arrangement** forming part of the **Security Amount** is due to expire within 9 **Business Days** immediately, and without notice to the **User**, demand payment of the entire amount of any outstanding **Letter of Credit** and/or ~~**Qualifying Guarantee**~~ and/or **Bilateral Insurance Policy** and/or **Insurance Performance Bond** and/or **Independent Security Arrangement** and shall credit the proceeds of the **Letter of Credit** and/or ~~**Qualifying Guarantee**~~ and/or **Bilateral Insurance Policy** and/or **Insurance Performance Bond** and/or **Independent Security Arrangement** to the **Escrow Account**.

3.21.7 Substitute ~~Letter of Credit or Qualifying Guarantee Security Cover~~

- (a) If the bank issuing the **User's Letter of Credit** ceases to have the credit rating set out in the definition of **Letter of Credit** in this **CUSC** such **User** shall forthwith procure the issue of a substitute **Letter of Credit** by a bank that has such a credit rating ~~or a **Qualifying Guarantee**~~ or a **Bilateral Insurance Policy** or an **Insurance Performance Bond** or an **Independent Security Arrangement** or transfer to **The Company** cash to be credited to the **Escrow Account**.
- ~~(b) If the entity providing the **User's Qualifying Guarantee** ceases to have an **Approved Credit Rating** for an amount at least equal to the required **Security Amount** (less the **User's** balance on the **Escrow Account**) the **User** shall forthwith procure a replacement **Qualifying Guarantee** from an entity with such a credit rating or a **Letter of Credit** or a **Bilateral Insurance Policy** or an **Insurance Performance Bond** or an **Independent Security Arrangement** or transfer to **The Company** cash to be credited to the **Escrow Account**.~~
- (eb) If the entity providing the **User's Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** ceases to meet the **Requirements** the **User** shall forthwith procure a replacement of the same or a **Bilateral Insurance Policy**, **Insurance Performance Bond**, **Independent Security Arrangement**, **Letter of Credit**, **Qualifying Guarantee** or transfer to **The Company** cash to be credited to the **Escrow Account**.

3.22 **CREDIT MONITORING**3.22.1 Determination of Security Cover

The amount of **Security Cover** which the **User** shall be required to maintain shall be determined from time to time by **The Company** as the **User's Security Requirement** less the **User's Allowed Credit**.

3.22.2 Determination of Security Requirement

**The Security Requirement for each User shall be determined as:-**

- (a) the **Balancing Services Use of System Charges** provided for in the **CUSC**, where the **User** is a **Supplier**, over a 32 day period or such period as **The Company** acting reasonably shall specify to the **User** in writing from time to time taking into account the requirements for **Security Cover** contained in the **Balancing and Settlement Code** and where **The Company** proposes to change such period **The Company** shall consult with **Users**; and
- (b) the **Balancing Services Use of System Charges** provided for in the **CUSC**, where the **User** is a **Generator**, over a 29 day period or such period as **The Company** acting

reasonably shall specify to the **User** in writing from time to time taking into account the requirements for **Security Cover** contained in the **Balancing and Settlement Code** and where **The Company** proposes to change such period **The Company** shall consult with **Users**; and

- (c) **Transmission Network Use of System Demand Charges** calculated in the following manner:-
- (aa) 10% of **User's Transmission Network Use of System Demand Charges** for the **Financial Year** in which such charges first become due; and
  - (bb) in the case of subsequent **Financial Years** such percentage of **User's Transmission Network Use of System Demand Charges** as reflects the percentage difference between the **Actual Amount** and the **Notional Amount** of the **User's Transmission Network Use of System Demand Charges** for the previous **Financial Year**, provided that where the **Notional Amount** exceeds the **Actual Amount**, the percentage shall be zero; and
- (d) interest on the amounts referred to in (a), (b) and (c) above calculated in accordance with the provisions of this **CUSC**.

### 3.22.3 Review of Security Cover

**The Company** shall keep under review the **Security Cover** relating to the **User** and shall promptly advise the **User** whenever the **Security Amount** maintained by the **User** is more or less than the amount required to be maintained pursuant to this Paragraph 3.22.

### 3.22.4 Decrease of Security Cover

If **The Company** reasonably determines that the **User's** required **Security Cover** has decreased, it shall so notify the **User**. **The Company** shall consent to an appropriate reduction in the available amount of any outstanding ~~Qualifying Guarantee or~~ **Letter of Credit** or **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** and/or shall repay to the **User** such part of the deposit held in the **Escrow Account** for the account of the **User** (together with all accrued interest on the part to be repaid) sufficient to reduce the **User's Security Amount** to the level of **Security Cover** applicable to it within 5 **Business Days** of the **User's** consent.

### 3.22.5 Notification in respect of Security Cover and Qualifying Guarantees

**The Company** shall notify each **User** promptly if:-

- (a) that **User** fails to provide, maintain, extend or renew a **Qualifying Guarantee** or a **Letter of Credit** or a **Bilateral Insurance Policy** or an **Insurance Performance Bond** or an **Independent Security Arrangement** which it is required

- to provide, maintain, extend or renew pursuant to Paragraphs 3.21 or 3.22 inclusive;
- (b) **The Company** shall make a demand under any such **Qualifying Guarantee** or a call under a **Letter of Credit** or a **Bilateral Insurance Policy** or an **Insurance Performance Bond** or an **Independent Security Arrangement**; or
- (c) **The Company** becomes aware that ~~that User~~:
- (i) ~~that User shall cease to have an **Approved Credit Rating** or, where the User holds an **Approved Credit Rating**, that User's specific investment grading shall change shall cease to have an **Approved Credit Rating** for an amount at least equal to the User's **Security Requirement**, or~~
- (ii) ~~where the **User's Allowed Credit** is provided by a **Qualifying Guarantee**, the **Parent Company** shall cease to have an **Approved Credit Rating**, or the **Parent Company's** specific investment grading shall change, or~~
- (iii) ~~that User shall be placed on a credit watch by the relevant credit rating agency (or becomes subject to an equivalent procedure) which in any case casts doubt on the User retaining an **Approved Credit Rating** or maintaining its existing investment grading an **Approved Credit Rating** for an amount at least equal to the User's **Security Requirement** or maintaining the **Credit Assessment Score** given by the User's **Independent Credit Assessment**, or~~
- (iv) ~~that User shall be in default under the additional or alternative security required to be provided pursuant to this Part III; or~~
- (d) **The Company** becomes aware that any bank that has issued a **Letter of Credit** in relation to that **User** which has not expired shall cease to have the credit rating required by this Section; or
- (e) **The Company** becomes aware that any entity providing a ~~**Qualifying Guarantee** or a **Bilateral Insurance Policy**~~ or an **Insurance Performance Bond** or an **Independent Security Arrangement** in relation to that **User** which has not expired shall cease to meet the **Requirements** ~~in the case of a **Bilateral Insurance Policy** or an **Insurance Performance Bond** or an **Independent Security Arrangement** or in the case of a **Qualifying Guarantee**~~ cease to have an **Approved Credit Rating** for an amount at least equal to the required **Security Amount** (less its balance on the **Escrow Account**); or
- (f) ~~**NGC**~~ ~~**The Company**~~ becomes aware that the **User's Security Requirement** exceeds 85% of the sum of the User's Allowed Credit and the Security Amount.

Provided always that the failure by **The Company** to notify the **User** pursuant to Paragraphs 3.22.3, 3.22.4 or 3.22.5 shall not relieve the **User** of its obligations under and in accordance with the terms of this Section 3 and the **Charging Statements**.

#### 3.22.6 Release from Security Cover Obligations

Upon a **User** becoming a **Dormant CUSC Party** or ceasing to be a **CUSC Party** and provided that all amounts owed by the **User** in respect of **Balancing Services Use of System Charges** and **Transmission Network Use of System Demand Charges** have been duly and finally paid and that it is not otherwise in default in any respect of any **Balancing Services Use of System Charges** or **Transmission Network Use of System Demand Charges** (including in each case interest) payable under the **CUSC**, the **User** shall be released from the obligation to maintain **Security Cover** and **The Company** shall consent to the revocation of any outstanding **Qualifying Guarantee** or **Letter of Credit** or a **Bilateral Insurance Policy** or an **Insurance Performance Bond** or an **Independent Security Arrangement** and shall repay to the **User** the balance (including interest credited thereto) standing to the credit of the **User** on the **Escrow Account** at that date.

### 3.23 PAYMENT DEFAULT

If, by 12.30 hours on any **Use of System Payment Date**, **The Company** has been notified by a **User** or it otherwise has reason to believe that that **User** will not have remitted to it by close of banking business on the **Use of System Payment Date** all or any part ("the amount in default") of any amount which has been notified by **The Company** to the **User** as being payable by the **User** by way of either the **Balancing Services Use of System Charges** and/or **Transmission Network Use of System Demand Charges** on the relevant **Use of System Payment Date**, then **The Company** shall be entitled to act in accordance with the following provisions (or whichever of them shall apply) in the order in which they appear until **The Company** is satisfied that the **User** has discharged its obligations in respect of the **Balancing Services Use of System Charges** and/or **Transmission Network Use of System Demand Charges** (as appropriate) under the **CUSC** which are payable in respect of the relevant **Settlement Day** (in the case of **Balancing Services Use of System Charges**) or **Financial Year** (in the case of **Transmission Network Use of System Demand Charges**):-

- (a) **The Company** may to the extent that the **User** is entitled to receive payment from **The Company** pursuant to the **CUSC** (unless it reasonably believes that such set-off shall be unlawful) set off the amount of such entitlement against the amount in default;
- (b) **The Company** shall be entitled to set off the amount of funds then standing to the credit of the **Escrow Account** against **Balancing Services Use of System Charges** and/or **Transmission Network Use of System Demand Charges** (as appropriate) unpaid by the **User** and for that purpose **The Company** shall be entitled to transfer any such amount from the **Escrow Account** to any other account of **The Company** at its absolute discretion and shall notify the **User** accordingly;



- (c) **The Company** may demand payment under any outstanding **Letter of Credit** supplied by the **User** in a sum not exceeding the available amount of all such **Letters of Credit**;
- (d) **The Company** may demand payment under any outstanding **Qualifying Guarantee** provided for the benefit of the **User** pursuant to Paragraph 3.21.3 (b);
- (e) **The Company** may demand payment under any outstanding **Bilateral Insurance Policy** provided for the benefit of the **User**;
- (g) **The Company** may demand payment under any outstanding **Insurance Performance Bond** provided for the benefit of the **User**;
- (h) **The Company** may demand payment under any outstanding **Independent Security Arrangement** provided for the benefit of the **User**.

### 3.24 UTILISATION OF FUNDS

In addition to the provisions of Paragraph 3.23 above if **The Company** serves a notice of default under the terms of Paragraph 5.5 or a notice of termination under Paragraph 5.7 then **The Company** shall be entitled to demand payment of any of the **Balancing Services Use of System Charges** and/or **Transmission Network Use of System Demand Charges** which are outstanding from the relevant **User** whether or not the **Use of System Payment Date** in respect of them shall have passed and:-

- (a) make demand under any outstanding **Qualifying Guarantee** or a call under any outstanding **Letter of Credit, Bilateral Insurance Policy, Insurance Performance Bond** or **Independent Security Arrangement** supplied by the **User**; and
- (b) to set off the funds in the **Escrow Account** against **Balancing Services Use of System Charges** and/or **Transmission Network Use of System Demand Charges** unpaid by the **User** and for that purpose **The Company** shall be entitled to transfer any such amount from the **Escrow Account** to any other account of **The Company** as it shall in its sole discretion think fit.

### 3.25 USER'S RIGHT TO WITHDRAW FUNDS

If a **User** is not in default in respect of any amount owed to **The Company** in respect of the **Balancing Services Use of System Charges** or **Transmission Network Use of System Charges** under the terms of the **CUSC** and any **Bilateral Agreement** to which the **User** is a party:-



- (a) **The Company** shall transfer to the **User** quarterly interest credited to the **Escrow Account**; and
- (b) **The Company** shall transfer to such **User** within a reasonable time after such **User's** written request therefore any amount of cash provided by the **User** by way of **Security Cover** which exceeds the amount which such **User** is required to provide by way of security in accordance with this Part III.

### 3.26 USER'S ALLOWED CREDIT

3.26.1 Each **User** shall notify ~~NGC~~The Company promptly if:-

- (a) it gains an **Approved Credit Rating**; or
- (b) it ceases to have an **Approved Credit Rating**; or
- (c) where the **User** holds an **Approved Credit Rating**, its specific investment grading changes; or
- (d) it has reason to believe that its **Credit Assessment Score** is likely to have changed since the last **Independent Credit Assessment**;  
or

(e) where the **User's Allowed Credit** is provided by a **Qualifying Guarantee**, the **Parent Company** ceases to have an **Approved Credit Rating**; or

(f) where the **User's Allowed Credit** is provided by a **Qualifying Guarantee**, the specific investment grading of the **Parent Company** changes.

3.26.2 ~~Subject to 3.26.10, t~~The **User's Allowed Credit** extended by ~~NGC~~The Company at any time to each **User** with an **Approved Credit Rating** shall be calculated in accordance with Paragraph 1 of Appendix 1 of this Section 3 subject to a maximum value of the **Unsecured Credit Cover**.

3.26.3 The **User's Allowed Credit** extended by ~~NGC~~The Company at any time to each **User** without an **Approved Credit Rating** shall be at the choice of the **User** the **Payment Record Sum**, ~~or~~ the **Credit Assessment Sum** or by way of a **Qualifying Guarantee** for an amount calculated and provided in accordance with Paragraph 3.26.10.

3.26.4 Unless the **User** has ~~requested otherwise notified NGC that it wishes its **User's Allowed Credit** to be to be based on the **Credit Assessment Sum**~~ then, subject to Paragraph 3.26.5, for each successive month in which the **User** pays its **Use of System Charges** by the **Use of System Payment Date** then the **User's Allowed Credit** extended to such **User** at any time shall be calculated in accordance with Paragraph 2 of Appendix 1 of this Section 3.

3.26.5 Where a **User** fails to pay its **Use of System Charges** within 2 **Business Days** of the **Use of System Payment Date** its **Payment Record Sum** shall be reduced by 50% on the first such occasion within a twelve month period and shall be reduced to zero on the second occasion in such twelve month period. Upon any such failure to pay, the **User's Allowed Credit** (as adjusted following such failure in accordance with this clause) shall be calculated for successive months in accordance with Paragraph 3.26.4.

- 3.26.6 Where a **User** has notified ~~NGC-The Company~~ that it wishes its **User's Allowed Credit** to be based on its **Credit Assessment Sum**, the **Credit Assessment Sum** extended to a User at any time shall be calculated by reference to the Credit Assessment Score given by the Independent Credit Assessment in accordance with Paragraph 3 of Appendix 1 of this Section 3.
- 3.26.7 Where a **User** has notified ~~NGC-The Company~~ that it wishes its **User's Allowed Credit** to be based on the **Credit Assessment Sum** then the **User** will obtain an **Independent Credit Assessment** of that **User**. The first such **Independent Credit Assessment** will be at ~~NGC's-The Company's~~ cost.
- 3.26.8 Where a **User's Allowed Credit** is based on the **Credit Assessment Sum** then where ~~NGC-The Company~~ has reason to believe that the **Independent Credit Assessment** last obtained is likely to have changed then ~~NGC-The Company~~ shall be entitled to request the **User** to obtain a further **Independent Credit Assessment**. Such **Independent Credit Assessment** shall be at ~~NGC's-The Company's~~ cost.
- 3.26.9 The **User** may obtain an **Independent Credit Assessment** at ~~NGC's-The Company's~~ cost provided that ~~The Company~~ has ~~NGC~~ not paid for an earlier **Independent Credit Assessment** for that User within the previous 12 months. The **User** may obtain further **Independent Credit Assessments** within such a 12 month period at the **User's** cost.
- 3.26.10 Subject to Paragraph 3.26.12, where the **User** has provided a **Qualifying Guarantee** for an amount calculated in accordance with Paragraph 1 of Appendix 1 of this Section 3, but substituting references to the **Parent Company** for references to the **User** in all such calculations and for the period of such **Qualifying Guarantee** then such amount shall constitute the **User Allowed Credit** for that **User**
- 3.26.11 Not later than 10 **Business Days** before any outstanding **Qualifying Guarantee** is due to expire, the **User** shall provide ~~The Company~~ with confirmation from the issuing entity that the validity of the **Qualifying Guarantee** has been extended for a period of not less than 6 months or shall provide ~~The Company~~ with a new **Qualifying Guarantee** which shall be available for a period of not less than 6 months.
- 3.26.12 Where a **Parent Company** provides a **Qualifying Guarantee** for more than one **User**, the aggregate of the value of all of the **Qualifying Guarantees** so provided shall not exceed the value of the maximum **User's Allowed Credit** calculated in accordance with Paragraph 1 of Appendix 1 of this Section 3, substituting the **Parent Company** for the **User** in all such calculations.

### 3.27 TRANSITIONAL ARRANGEMENTS

Recognising the changes to the **Security Cover** and **Security Requirements** introduced by the **Security Amendment** and the consequences for ~~NGC-The Company~~ and **Users** then notwithstanding the provisions of **CUSC** Section 3 Part III the following transitional provisions shall apply:

- (a) the obligation for **Users** whose **Security Requirement** will as a result of the **Security Amendment** increase at the **Security Amendment Implementation Date** shall be to provide the difference between the **Existing Security Cover** and the **Security**

**Cover** in full by no later than the **End Date** and by increasing the **Existing Security Cover** each month by equal monthly amounts of the difference between the existing **Security Cover** and the **Security Cover**; and

- (b) where a **User's Security Requirement** at the **Security Amendment Implementation Date** is less than the **Existing Security Cover** held for that **User** then **NHC-The Company** shall release the existing **Security Cover** by the appropriate amount as soon as practicable and in any event within one calendar month of the **Security Amendment Implementation Date**.

**APPENDIX 1 CREDIT ARRANGEMENTS**

- 1 Where the **User** meets the **Approved Credit Rating** that **User's Allowed Credit** at any given time shall be calculated as a percentage of **Unsecured Credit Cover** by reference to the specific investment grade within the **User's Approved Credit Rating** as follows:

Approved Long Term Credit Rating			User's Allowed Credit as % of Unsecured Credit Cover
Standard & Poor's	Moody's	Fitch	
AAA AA+ AA AA-	Aaa Aa1 Aa2 Aa3	AAA AA+ AA AA-	100
A+ A A-	A1 A2 A3	A+ A A-	40
BBB+	Baa1	BBB+	20
BBB	Baa2	BBB	19
BBB-	Baa3	BBB-	18
BB+	Ba1	BB+	17
BB	Ba2	BB	16
BB-	Ba3	BB-	15

- 2 Where based on the **Payment Record Sum**, a **User's Allowed Credit** at any time shall be calculated on the basis of 0.4% per 12 month period (escalating on an evenly graduated basis each month) of the **Unsecured Credit Cover**, subject to a maximum of 2% after 60 months of successive payment by the **Use of System Payment Date**.
- 3 Where based on the **Credit Assessment Sum**, a **User's Allowed Credit** at any given time shall be calculated as a percentage of the **Unsecured Credit Cover** by reference to the **Credit Assessment Score** as follows:

Credit Assessment Score	User's Allowed Credit as % of Unsecured Credit Cover
10	20
9	19
8	18
7	17
6	16
5	15
4	13.33
3	10
2	6.67
1	3.33
0	0

**END OF SECTION 3**

## Section 11

## DEFINITIONS AND INTERPRETATION

<b>“Independent Security Arrangement”</b>	a guarantee in favour of <b>The Company</b> in a form satisfactory to <b>The Company</b> and which is provided by an entity <u>other than a <b>Parent Company</b></u> which meets the <b>Requirements</b> . In addition <b>The Company</b> may accept such a policy from an entity <u>other than a <b>Parent Company</b></u> who does not meet the <b>Requirements</b> up to an <b>Agreed Value</b> where <b>The Company</b> agrees or where <b>The Company</b> does not agree as determined by an expert appointed by <b>The Company</b> and the <b>User</b> or failing their agreement as to the expert the expert nominated by the Director General of The Institute of Credit Management;
<b><u>“Parent Company”</u></b>	<u>a company which is a public company or a private company within the meaning of section 1(3) of the Companies Act 1985 and which is either a shareholder of the User or any holding company of such shareholder (the expression holding company having the meaning assigned thereto by section 736, Companies Act 1985 as supplemented by section 144(3), Companies Act 1989);</u>
<b>“Qualifying Guarantee”</b>	a guarantee in favour of <b>The Company</b> in a form proposed by the <b>User</b> and agreed by <b>The Company</b> (whose agreement shall not be unreasonably withheld or delayed) and which is <u>valid for a period of not less than six months and provided by <del>a Parent Company</del>—an entity</u> which holds an <b>Approved Credit Rating</b> <del>provided that such guarantee cannot secure a sum greater than the level of <b>User’s Allowed Credit</b> that would be available to that entity in accordance with Paragraph 3.26 if it was a <b>User</b>;</del>
<b>“Security Amount”</b>	in respect of the <b>User</b> the aggregate of available amounts of each outstanding (a) <b>Letter of Credit</b> , (b) <u><b>Qualifying Guarantee Bilateral Insurance Policy</b>, (c) <b>Insurance Performance Bond</b>, (d) <b>Independent Security Arrangement</b></u> and (ee) the principal amount (if any) of cash that the <b>User</b> has paid to the credit of the <b>Escrow Account</b> (and which has not been repaid to the <b>User</b> ); for the purpose of this definition, in relation to a <b>Letter of Credit</b> or <u><b>Qualifying Guarantee Bilateral Insurance Policy or Insurance Performance Bond or Independent Security Arrangement</b></u> “available amount” means the face amount thereof less (i) payments already made thereunder and (ii) claims made thereunder but not yet paid;

**ANNEX 2 – AMENDMENT PROPOSAL FORM**

<b>CUSC Amendment Proposal Form</b>	<b>CAP:126</b>
<b>Title of Amendment Proposal:</b>	
Clarification of the applicability and definition of Qualifying Guarantee and Independent Security	
<b>Description of the Proposed Amendment</b> (mandatory by proposer):	
<p>Currently within CUSC Section 3, a ‘<b>Qualifying Guarantee</b>’ and ‘<b>Independent Security Arrangement</b>’ are open to misinterpretation.. The proposal seeks to rectify this issue and better align the CUSC to the original intention of Ofgem’s Best Practice Guidelines, making the two elements mutually exclusive in that a company will only be able to provide one or the other to a user.</p> <p>The changes can be summarised as:</p> <p><b>Clarification of Qualifying Guarantee</b></p> <ul style="list-style-type: none"> <li>• To move <b>Qualifying Guarantees</b> from being Collateral (i.e. part of the Security Amount) to instead determining the <b>User’s Allowed Credit</b>;</li> <li>• To clarify that these <b>Qualifying Guarantees</b> can only be provided by a “<b>Qualifying Company</b>” (Parent Companies); and</li> <li>• To clarify that where a “<b>Qualifying Company</b>” (Parent Companies) provides <b>Qualifying Guarantees</b> for more than one User, the <b>Qualifying Guarantees</b> in aggregate cannot exceed the value of <b>User’s Allowed Credit</b> that would be extended to the Parent Company if it were a User.</li> </ul> <p><b>Clarification of Independent Security</b></p> <ul style="list-style-type: none"> <li>• Independent Security <b>can only be provided by entities other than a “Qualifying Company” ( Parent Companies)</b></li> </ul>	
<b>Description of Issue or Defect that Proposed Amendment seeks to Address</b> (mandatory by proposer):	
<p>There are currently several issues with the application of <b>Qualifying Guarantees</b> in the security arrangements, these are;</p> <ul style="list-style-type: none"> <li>• They are treated as a collateral tool and not an allowance. Where a user has a rating that does not afford it an allowance greater than its requirement it is using its Parent Company’s allowance as an additional collateral tool. The user should instead substitute its allowance with that of its Parent Company.</li> <li>• They can be given by a party which is not a direct parent.</li> <li>• A single <b>Qualifying Company</b> can provide many guarantees in excess of its maximum allowance.</li> <li>• The issue with the <b>Independent Security Arrangement</b> is that it is not clear that it should be issued by anyone other than a <b>Qualifying Company</b>.</li> </ul>	
<b>Impact on the CUSC</b> (this should be given where possible):	
Section 3 Part III (Credit Requirements), Section 6 (General Provisions) and Section 11 (Interpretation and Definitions)	

<p><b>Impact on Core Industry Documentation</b> (this should be given where possible):</p> <p>None anticipated</p>
<p><b>Impact on Computer Systems and Processes used by CUSC Parties</b> (this should be given where possible):</p> <p><b>None anticipated</b></p>
<p><b>Details of any Related Modifications to Other Industry Codes</b> (where known):</p> <p>N/A</p>
<p><b>Justification for Proposed Amendment with Reference to Applicable CUSC Objectives**</b> (mandatory by proposer):</p> <p><b>National Grid believes that this proposal will better facilitate CUSC Applicable Objectives;</b></p> <p><b>(a) the efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence; and</b></p> <p><b>(b) facilitating effective competition in the generation and supply of electricity, and (so far as consistent therewith) facilitating such competition in the sale, distribution and purchase of electricity;</b></p> <p>by clarifying the applicability and definition of Qualifying Guarantee and Independent Security, CUSC parties are able to make a more informed decision on the use of credit allowances and collateral tools available to manage their security obligations.</p>

<p><b>Details of Proposer:</b> Organisation's Name:</p>	National Grid
<p><b>Capacity in which the Amendment is being proposed:</b> (i.e. CUSC Party, BSC Party or "energywatch")</p>	CUSC Party
<p><b>Details of Proposer's Representative:</b> Name: Organisation: Telephone Number: Email Address:</p>	<p><i>Paul Murphy</i> <i>National Grid Electricity Transmission</i> <i>01926 656330</i> <i>Paul.Murphy@uk.ngrid.com</i></p>
<p><b>Details of Representative's Alternate:</b> Name: Organisation: Telephone Number: Email Address:</p>	<p><i>Bec Thornton</i> <i>National Grid Electricity Transmission</i> <i>01926 65686</i> <i>Bec.Thornton@uk.ngrid.com</i></p>
<p><b>Attachments (Yes/No):</b> <b>If Yes, Title and No. of pages of each Attachment:</b></p>	No

**Notes:**

1. Those wishing to propose an Amendment to the CUSC should do so by filling in this "Amendment Proposal Form" that is based on the provisions contained in Section 8.15 of the CUSC. The form seeks to ascertain details about the Amendment Proposal so that the Amendments Panel can determine more clearly whether the proposal should be considered by a Working Group or go straight to wider National Grid Consultation.
2. The Panel Secretary will check that the form has been completed, in accordance with the requirements of the CUSC, prior to submitting it to the Panel. If the Panel Secretary accepts the Amendment Proposal form as complete, then he will write back to the Proposer informing him of the reference number for the Amendment Proposal and the date on which the Proposal will be considered by the Panel. If, in the opinion of the Panel Secretary, the form fails to provide the information required in the CUSC, then he may reject the Proposal. The Panel Secretary will inform the Proposer of the rejection and report the matter to the Panel at their next meeting. The Panel can reverse the Panel Secretary's decision and if this happens the Panel Secretary will inform the Proposer.

The completed form should be returned to:

Beverley Viney  
Panel Secretary  
Commercial Frameworks  
National Grid Company plc  
NGT House  
Warwick Technology Park  
Gallows Hill  
Warwick, CV34 6DA  
Or via e-mail to: [Beverley.viney@uk.ngrid.com](mailto:Beverley.viney@uk.ngrid.com)

(Participants submitting this form by email will need to send a statement to the effect that the proposer acknowledges that on acceptance of the proposal for consideration by the Amendments Panel, a proposer which is not a CUSC Party shall grant a licence in accordance with Paragraph 8.15.7 of the CUSC. A Proposer that is a CUSC Party shall be deemed to have granted this Licence).

3. Applicable CUSC Objectives\*\* - These are defined within the National Grid Company Transmission Licence under Section C10, paragraph 1. Reference should be made to this section when considering a proposed amendment.



**ANNEX 3 – REPRESENTATIONS RECEIVED DURING CONSULTATION**

This Annex includes copies of any representations received following circulation of the Consultation Document (circulated on 7<sup>th</sup> December 2006, requesting comments by close of business on 3<sup>rd</sup> January 2007).

Representations were received from the following parties:

Beverley Viney  
Amendments Panel Secretary  
Electricity Codes  
National Grid

By email: Beverley.Viney@uk.ngrid.com

**E.ON UK plc**  
Westwood Way  
Westwood Business Park  
Coventry  
CV4 8LG  
eon-uk.com

Ben Sheehy  
024 7618 3381

ben.sheehy@eon-uk.com

No.	Company	File Number
1	E.ON UK	CAP126-CR-01

<b>Reference</b>	CAP126-CR-01
<b>Company</b>	E.ON UK



Tuesday 2 January 2007

Dear Beverley,

**Consultation Response: CAP126, Clarification of the Applicability and Definition of Qualifying Guarantee and Independent Security**

Thank you for the opportunity to comment on the CAP126 consultation document. Please note that, on behalf of E.ON UK, I concur with National Grid's view that the Amendment Proposal would better facilitate achievement of the Applicable CUSC Objectives (a) and (b). Furthermore, it would bring an area of network operator credit cover into line with best practice guidelines, as published in 2005.

Yours sincerely,

Ben Sheehy

Trading Arrangements  
Energy Wholesale

E.ON UK plc  
Registered in  
England and Wales  
No 2366970

Registered Office:  
Westwood Way  
Westwood Business Park  
Coventry CV4 8LG