



WORKING GROUP REPORT

CUSC Amendment Proposal CAP126 Clarification of the Applicability and Definition of Qualifying Guarantee and Independent Security

**Prepared by the CAP126 Working Group
for submission to the Amendments Panel**

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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 certain elements of these guidelines, CAP099 was implemented November 2005. Following CAP099, Ofgem considered that there were particular areas that still needed further work. 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 was raised by National Grid and was considered by the CUSC Amendments Panel on 29th September 2006 where it was agreed that a Working Group should consider the proposals. The Working Group were required to report back to the November 2006 Panel meeting but its terms of reference required that if the Group reached agreement before this then it should submit the report earlier than this.

Working Group Recommendation

- 1.3 The Working Group believes its Terms of Reference have been completed. CAP126 has been fully considered and recommends to the CUSC Panel that the proposal should proceed to wider Industry Consultation as soon as possible.

2.0 PURPOSE AND INTRODUCTION

- 2.1 This report summarises the deliberations of the Working Group and describes the CAP126 proposal.
- 2.2 CAP126 was proposed on and submitted to the Amendments Panel for their consideration on 29th September 2006. The Amendments Panel determined that the proposal should be considered by a Working Group and that the Group should report back to the Panel within 2 months.
- 2.3 The Working Group met on 18th October 2006 and 1st November 2006 at National Grid's offices and the members accepted the Terms of Reference for CAP126. A copy of the Terms of Reference is provided in Annex 2. The Working Group considered the issues raised by the Amendment Proposal and considered whether the Proposal better facilitated the Applicable CUSC Objectives.
- 2.4 This Working Group Report has been prepared in accordance with the Terms of the CUSC. An electronic copy can be found on the National Grid Website, www.nationalgrid.com/uk/Electricity/Codes/, along with the Amendment Proposal Form.

3.0 PROPOSED AMENDMENT

3.1 Ofgem's best practice guidelines recommended that a number of additional collateral tools should be available to counterparties of gas and electricity network operators to allow them to cover any security requirements beyond their unsecured credit limit. In addition to a Letter of Credit and Cash held in an Escrow account CAP099 implemented the use of:

- A Performance Bond (provided by an insurance company, not a bank)
- Bilateral Insurance
- Independent Security

3.2 CAP126 proposes to amend the CUSC to clarify the definition and use of Independent Security.

3.3 In addition, CAP126 proposes to clarify the definition and use of Qualifying Guarantees.

3.4 For the avoidance of doubt, the scope of these proposals is limited to the provision of security for Demand Use of System charges. Please also note that Standard and Poor's long term credit ratings are used throughout this document; such references should be read as allowing equivalent short term ratings or equivalent long or short term ratings from Moody's or Fitch.

4.0 SUMMARY OF WORKING GROUP DISCUSSIONS

4.1 The Working Group considered CAP126, the results the discussions are summarised below:

Qualifying Guarantee

4.2 National Grid explained that Qualifying Guarantees are currently:

- being provided by parties which are not direct parents of User;
- being treated as collateral and not an allowance; and
- being provided in excess of a parent company's maximum allowance.

4.3 The Working Group clarified and agreed that Qualifying Guarantees could:

- only be provided from a Parent Company;
- only 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 of the CUSC.

Independent Security

4.4 National Grid explained that Independent Security can currently:

- be provided by a parent company as collateral to a direct subsidiary.

4.5 The Working Group clarified and agreed that Independent Security could:

- only be issued from anyone other than a Parent Company;
- only be used as a collateral tool; and
- only be issued by Parent Companies to non-subsidiaries.

Summary and Legal Text

4.6 The Working Group agreed that clarifying the definition and application of Independent Security and Qualifying Guarantee would better meet the Applicable CUSC Objectives by removing any ambiguity and risk of double counting and thus under securitisation.

4.7 The Working Group reviewed and approved the legal text to give effect to CAP126, which is attached as Annex 1 of this document.

5.0 WORKING GROUP ALTERNATIVE AMENDMENTS

5.1 No Alternative Amendments were raised.

6.0 ASSESSMENT AGAINST APPLICABLE CUSC OBJECTIVES

6.1 The Working Group believed that CAP126 would better meet the Applicable CUSC Objectives. These can be summarised as follows:

- (a) the efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence; and
- (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.

6.2 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.

6.3 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.

7.0 PROPOSED IMPLEMENTATION

7.1 It is proposed that should the Authority approve the CAP126 proposal, implementation should be 10 Business Days after the Authority decision.

8.0 IMPACT ON CUSC

- 8.1 The CAP126 proposal will require a number of changes to Section 3 of the CUSC Part III Credit Requirements.
- 8.2 The text to give effect to the CAP126 Proposal is contained In Annex 1 to this document.

9.0 IMPACT ON INDUSTRY DOCUMENTS

Impact on Core Industry Documents

- 9.1 CAP126 has no impact no impact on other Core Industry Documents.

Impact on other Industry Documents

- 9.2 CAP126 has no impact on other Industry Documents.

Annex 1 – Legal Text

The proposed Legal text to modify the CUSC Section 3 is detailed below deleting the coloured struck through text and inserting the coloured underlined text.

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~~

(i) 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

(ii) 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

(iii) 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~~

(~~c~~) 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**;
- (g) **The Company** may demand payment under any outstanding **Qualifying Guarantee** provided for the benefit of the **User** pursuant to Paragraph 3.26.10;
- (h) **The Company** may demand payment under any outstanding **Bilateral Insurance Policy** provided for the benefit of the **User**;
- (i) **The Company** may demand payment under any outstanding **Insurance Performance Bond** provided for the benefit of the **User**;
- (j) **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 therefor 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~~
- (e) 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~~he **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 ~~Company has NGC-The~~ 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 **~~NHC~~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	Aaa	AAA	100
AA+	Aa1	AA+	
AA	Aa2	AA	
AA-	Aa3	AA-	
A+	A1	A+	40
A	A2	A	
A-	A3	A-	
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

“Independent Security Arrangement”

a guarantee in favour of **The Company** in a form satisfactory to **The Company** and which is provided by an entity other than a Parent Company which meets the **Requirements**. In addition **The Company** may accept such a policy from an entity other than a Parent Company who does not meet the **Requirements** up to an **Agreed Value** where **The Company** agrees or where **The Company** does not agree as determined by an expert appointed by **The Company** and the User or failing their agreement as to the expert the expert nominated by the Director General of The Institute of Credit Management;

“Parent Company”

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);

“Qualifying Guarantee”

a guarantee in favour of **The Company** in a form proposed by the **User** and agreed by **The Company** (whose agreement shall not be unreasonably withheld or delayed) and which is valid for a period of not less than six months and provided by a Parent Company ~~an entity~~ which holds an **Approved Credit Rating** ~~provided that such guarantee cannot secure a sum greater than the level of User’s Allowed Credit that would be available to that entity in accordance with Paragraph 3.26 if it was a User;~~

“Security Amount”

in respect of the **User** the aggregate of available amounts of each outstanding (a) **Letter of Credit**, (b) ~~Qualifying Guarantee~~ **Bilateral Insurance Policy**, (c) **Insurance Performance Bond**, (d) **Independent Security Arrangement** and (e) the principal amount (if any) of cash that the **User** has paid to the credit of the **Escrow Account** (and which has not been repaid to the **User**); for the purpose of this definition, in relation to a **Letter of Credit** or ~~Qualifying Guarantee~~ **Bilateral Insurance Policy** or **Insurance Performance Bond** or **Independent Security Arrangement** “available amount” means the face amount thereof less (i) payments already made thereunder and (ii) claims made thereunder but not yet paid;

Annex 2 – Working Group Terms of Reference and Membership

TERMS OF REFERENCE FOR CAP126 WORKING GROUP

RESPONSIBILITIES

1. The Working Group is responsible for assisting the CUSC Amendments Panel in the evaluation of CUSC Amendment Proposal CAP126 tabled by National Grid at the Amendments Panel meeting on 29 September 2006.
2. The proposal must be evaluated to consider whether it better facilitates achievement of the applicable CUSC objectives. These can be summarised as follows:
 - (a) the efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence; and
 - (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.
3. It should be noted that additional provisions apply where it is proposed to modify the CUSC amendment provisions, and generally reference should be made to the Transmission Licence for the full definition of the term.

SCOPE OF WORK

4. The Working Group must consider the issues raised by the Amendment Proposal and consider if the proposal identified better facilitates achievement of the Applicable CUSC Objectives.
5. In addition to the overriding requirement of paragraph 4, the Working Group shall consider and report on the following specific issues:
 - *Clarification of Independent Security as:*
 - o *issued from anyone other than a Parent Company*
 - o *Parent Company Guarantees issued only to subsidiaries; therefore Parent Companies can only issue Independent Security to non subsidiaries*
 - o *only use as a collateral tool*
 - *Clarification of Qualifying Guarantee as:*
 - o *from a Parent Company only*
 - o *use as an allowance rather than collateral*
 - o *aggregation of PCG allowance to maximum allowance.*
6. The Working Group is responsible for the formulation and evaluation of any Working Group Alternative Amendments (WGAAs) arising from Group discussions which would, as compared with the Amendment Proposal, better facilitate achieving the applicable CUSC objectives in relation to the issue or defect identified.

7. The Working Group should become conversant with the definition of Working Group Alternative Amendments which appears in Section 11 (Interpretation and Definitions) of the CUSC. The definition entitles the Group and/or an individual Member of the Working Group to put forward a Working Group Alternative Amendment if the Member(s) genuinely believes the Alternative would better facilitate the achievement of the Applicable CUSC Objectives. The extent of the support for the Amendment Proposal or any Working Group Alternative Amendment arising from the Working Group's discussions should be clearly described in the final Working Group Report to the CUSC Amendments Panel.
8. The Working Group is to submit their final report to the CUSC Panel Secretary on 16 November 2006 for circulation to Panel Members. The conclusions will be presented to the CUSC Panel meeting on 24 November 2006.

MEMBERSHIP

9. It is recommended that the Working Group has the following members:

Chair	Hedd Roberts
National Grid	Paul Murphy Wayne Mullins Bec Thornton
Industry Representatives	Andrew Colley Mark De Souza Keith Munday Paul Mott Ben Sheehy Dave Wilkerson Carl Wilkes
Authority Representative	Jenny Boothe
Technical Secretary	Dipen Gadhia Beverley Viney

[NB: Working Group must comprise at least 5 Members (who may be Panel Members) and will be selected by the Panel with regard to WG List held by the Secretary]

10. The membership can be amended from time to time by the CUSC Amendments Panel.

RELATIONSHIP WITH AMENDMENTS PANEL

11. The Working Group shall seek the views of the Amendments Panel before taking on any significant amount of work. In this event the Working Group Chairman should contact the CUSC Panel Secretary.
12. Where the Working Group requires instruction, clarification or guidance from the Amendments Panel, particularly in relation to their Scope of Work, the Working Group Chairman should contact the CUSC Panel Secretary.

MEETINGS

13. The Working Group shall, unless determined otherwise by the Amendments Panel, develop and adopt its own internal working procedures and provide a copy to the Panel Secretary for each of its Amendment Proposals.

REPORTING

14. The Working Group Chairman shall prepare a final report to the November 2006 Amendments Panel responding to the matter set out in the Terms of Reference.
15. A draft Working Group Report must be circulated to Working Group members with not less than five business days given for comments.
16. Any unresolved comments within the Working Group must be reflected in the final Working Group Report.
17. The Chairman (or another member nominated by him) will present the Working Group report to the Amendments Panel as required.

Annex 3 – Internal Working Group Procedure

CAP126 Working Group

INTERNAL WORKING PROCEDURES

1. Notes and actions from each meeting will be produced by the Technical Secretary (provided by National Grid) and circulated to the Chairman and Working Group members for review.
2. The Meeting notes and actions will be published on the National Grid CUSC Website after they have been agreed at the next meeting or sooner on agreement by Working Group members.
2. The Chairman of the Working Group will provide an update of progress and issues to the Amendments Panel each month as appropriate.
4. Working Group meetings will be arranged for a date acceptable to the majority of members and will be held as often as required as agreed by the Working Group in order to respond to the requirements of the Terms of Reference set by the Amendments Panel.
5. If within half an hour after the time for which the Working Group meeting has been convened the Chairman of the group is not in attendance, the meeting will take place with those present.
6. A meeting of the Working Group shall not be invalidated by any member(s) of the group not being present at the meeting.

Annex 4 – Amendment Proposal Form

CUSC Amendment Proposal Form	CAP:126
Title of Amendment Proposal:	
Clarification of the applicability and definition of Qualifying Guarantee and Independent Security	
Description of the Proposed Amendment <i>(mandatory by proposer):</i>	
<p>Currently within CUSC Section 3, a ‘Qualifying Guarantee’ and ‘Independent Security Arrangement’ 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>Clarification of Qualifying Guarantee</p> <ul style="list-style-type: none"> • To move Qualifying Guarantees from being Collateral (i.e. part of the Security Amount) to instead determining the User’s Allowed Credit; • To clarify that these Qualifying Guarantees can only be provided by a “Qualifying Company” (Parent Companies); and • To clarify that where a “Qualifying Company” (Parent Companies) provides Qualifying Guarantees for more than one User, the Qualifying Guarantees in aggregate cannot exceed the value of User’s Allowed Credit that would be extended to the Parent Company if it were a User. <p>Clarification of Independent Security</p> <ul style="list-style-type: none"> • Independent Security can only be provided by entities other than a “Qualifying Company” (Parent Companies) 	
Description of Issue or Defect that Proposed Amendment seeks to Address <i>(mandatory by proposer):</i>	
<p>There are currently several issues with the application of Qualifying Guarantees in the security arrangements, these are;</p> <ul style="list-style-type: none"> • 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. • They can be given by a party which is not a direct parent. • A single Qualifying Company can provide many guarantees in excess of its maximum allowance. • The issue with the Independent Security Arrangement is that it is not clear that it should be issued by anyone other than a Qualifying Company. 	
Impact on the CUSC <i>(this should be given where possible):</i>	
Section 3 Part III (Credit Requirements), Section 6 (General Provisions) and Section 11 (Interpretation and Definitions)	

<p>Impact on Core Industry Documentation <i>(this should be given where possible):</i></p> <p>None anticipated</p>
<p>Impact on Computer Systems and Processes used by CUSC Parties <i>(this should be given where possible):</i></p> <p>None anticipated</p>
<p>Details of any Related Modifications to Other Industry Codes <i>(where known):</i></p> <p>N/A</p>
<p>Justification for Proposed Amendment with Reference to Applicable CUSC Objectives** <i>(mandatory by proposer):</i></p> <p>National Grid believes that this proposal will better facilitate CUSC Applicable Objectives;</p> <p>(a) the efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence; and</p> <p>(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;</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>Details of Proposer: Organisation's Name:</p>	National Grid
<p>Capacity in which the Amendment is being proposed: (i.e. CUSC Party, BSC Party or "energywatch")</p>	CUSC Party
<p>Details of Proposer's Representative: Name: Organisation: Telephone Number: Email Address:</p>	<p>Paul Murphy National Grid Electricity Transmission 01926 656330 Paul.Murphy@uk.ngrid.com</p>
<p>Details of Representative's Alternate: Name: Organisation: Telephone Number: Email Address:</p>	<p>Bec Thornton National Grid Electricity Transmission 01926 65686 Bec.Thornton@uk.ngrid.com</p>
<p>Attachments (Yes/No): If Yes, Title and No. of pages of each Attachment:</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

(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.