CUSC Workgroup Consultation Response Proforma

CMP311 Reassessment of CUSC credit requirements for Suppliers, specifically for "User Allowed Credit" as defined in Section 3, Part III section 3.27 of the CUSC

Industry parties are invited to respond to this consultation expressing their views and supplying the rationale for those views, particularly in respect of any specific questions detailed below.

Please send your responses by **29 October 2019** to cusc.team@nationalgrideso.com Please note that any responses received after the deadline or sent to a different email address may not receive due consideration by the Workgroup.

Any queries on the content of the consultation should be addressed to Chrissie Brown at christine.brown1@nationalgrideso.com

These responses will be considered by the Workgroup at their next meeting at which members will also consider any Workgroup Consultation Alternative Requests. Where appropriate, the Workgroup will record your response and its consideration of it within the final Workgroup Report which is submitted to the CUSC Modifications Panel.

Respondent:	Richard Jerreat (Richard.jerreat@edfenergy.com)
Company Name:	EDF Energy Customers Limited
Please express your views regarding the Workgroup Consultation, including rationale. (Please include any issues, suggestions or queries)	**For reference, the Applicable CUSC Objectives for the Use of System** (a)The efficient discharge by the Licensee of the obligations imposed on it by the Act and the Transmission Licence; (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; (c)Compliance with the Electricity Regulation and any relevant legally binding decision of the European Commission and/or the Agency *; and (d) Promoting efficiency in the implementation and administration of the CUSC arrangements. **Objective (c) refers specifically to European Regulation 2009/714/EC. Reference to the Agency is to the Agency for the Cooperation of Energy Regulators (ACER).*

Standard Workgroup consultation questions

1	**Do you believe that CMP311 Original proposal (revised since originally proposed to just remove the Payment Record Sum) better facilitates the Applicable CUSC Objectives than current arrangements?**	(a) Yes, we believe it better facilitates this objective as NGESO needs to have sufficient financial resources available to it to fulfil its duties. Any incurred losses, even if they can be later reclaimed, could jeopardise this if those losses are larger than experienced to date (given NGESO's business model). NGESO also needs to play its part in maintaining an efficient and economical system; it is not efficient if multiple losses are incurred from failing Suppliers and subsequently claimed back from non-defaulting Suppliers and ultimately consumers. Set against this, it would be negative if Suppliers' credit cover costs increased substantially, if that was without justification in terms of the risks Suppliers place on the system. Overall, we see this modification proposal as positive. (b) On balance, we feel the impact on this objective is positive. We believe that independent credit assessments (an option that will remain available to Suppliers) are likely to be a better guide to a Supplier's credit-worthiness than payment history and, as a result, less credit-worthy Suppliers are more likely to have to provide collateral. This could reduce market entry, albeit it is more likely to ensure Suppliers bear their appropriate share of the risks to ensure effective competition. The changes would be more likely to prevent losses being passed on to the non-defaulting Suppliers, and ultimately consumers, and this could facilitate a more effective industry and improve consumer engagement and therefore competition. There are ultimate costs to consumers as a result of Supplier failures and if there are unsecured losses to ESO that are passed on, this does not present a picture of an industry that is operating effectively. (c) Neutral (d) We see the impact here as positive. Removing the requirement to administer the payment history element of the credit arrangements should improve efficiency. This may be partially offset by an increase in the use of independent credit assessments but this would likely be outweighed by the reduction in the hazard that comes from making unsecured allowances based on payment history.

2	**Do you support the proposed implementation approach, both in terms of allowing at least 12 months to make arrangements and the Workgroup suggestion to commence in April with the Financial Year?**	We support the proposal to allow at least 12 months to make alternative arrangements, but suggest 15 assuming no delay to April of the year. Waiting until April to commence with the financial year is fine if that only adds an extra month or two to the implementation phase but if that adds multiple months (potentially taking the total number up to 23 months) we do not feel that is appropriate. Not all Suppliers manage their financial arrangements based on an April start date, and companies do not have to wait until an April date to commence new arrangements. This is why we feel that allowing 15 months would be even more appropriate from decision date, e.g. if a Supplier manages its facilities annually, and the annual renewal is due just after a formal decision on this proposal, then it is unlikely that the Supplier could arrange changes that quickly, whereas it should be able to do so before the next annual renewal.

3	**Do you have any other comments?**	We believe it is sensible to review the credit arrangements and to focus on payment history allowance, which has caused the losses to date. Although Ofgem has confirmed that the best practice guidelines still apply, the industry has changed a lot since their publication. In addition, those guidelines recognised that the payment record of a company is not a strong positive indicator of its health and this has now been evidenced with losses in recent months. Independent credit assessments and approved credit ratings are specifically designed as indicators of creditworthiness, and are more robust. We have some concerns that a significant increase in the use of independent credit assessments could give risk to an increased build-up of risk for that category, particularly as some agencies take into account less factors (and are less robust) than others in their credit assessment processes. However, NGESO's empirical evidence has only shown losses arising through the payment history allowance category and so we feel it is fair to focus only on that category in this proposal. We also note that Ofgem, in its Supplier licensing review proposals for entry requirements, states that Suppliers should adopt effective risk management, be adequately prepared and resourced for growth, and bear an appropriate share of their risk. Based on the information available, we do not feel that the Suppliers which defaulted were bearing an appropriate share of their risk under the current credit arrangements. We therefore agree that there is a case for change.
4	**Do you wish to raise a Workgroup Consultation Alternative Request for the Workgroup to consider?**	No

Specific questions for CMP311

Q	Question	Response
5	**What impact do you think this modification would have on suppliers entering the market?**	We think this modification would require most new entrants - those that are unable to rely on an independent credit assessment, or provide a parent company guarantee from a parent with an approved credit rating, from the outset - to have access to greater collateral than they otherwise would. We do note though that new entrants will already be subject to greater scrutiny of their business plans and financial viability under Ofgem's entry requirement proposals, and Suppliers are already required to have access to collateral under certain industry arrangements anyway; this is therefore an incremental impact, rather than an entirely new one.
6	**What impact do you think this modification would have on existing suppliers and what would be the cost to your business?**	We think the impact would be a greater uptake of the independent credit assessment and/or provision of collateral, for those Suppliers that currently rely on payment history allowance. We do not know what this impact would be, as it will depend what credit line Suppliers can achieve via an independent credit assessment rather than payment history allowance. EDF Energy Customers Ltd currently relies on its approved credit rating, rather than payment history allowance, so there would be no immediate cost impact arising from this modification.

7	**Two potential solutions other than that Proposed have been discussed by the Workgroup, what are your views on these?**	We believe that NGESO's revised proposal should be implemented; however, if that is not approved then we believe potential alternative (potential WACM) A identified at the workgroup could have some merit, as it could help alleviate potential negative impacts of the revised modification i.e. (i) some new entrants not being able to gain access to a viable independent credit assessment for the first two years if they are start-up businesses and (ii) increased costs associated with extra collateral having to be provided. The potential alternatives would both effectively provide a two-year grace period for new entrants during which good payment history would still be allowed. This does create extra risk, over and above NGESO's revised proposal to remove payment history allowances entirely, particularly if Suppliers grow quickly in the first two years, but we feel this could be a practical way of addressing any barrier to entry considerations, if those are deemed to be material. Given this period would create risks, we feel two years is appropriate, not three, and two years also aligns with Ofgem's entry requirements proposals, whereas three years goes beyond that. Of the two potential alternatives, we would only support A (as the fallback) as it utilises the existing available credit options, which is better for efficiency. The extra feature of B is that it also suggests that Suppliers that would receive zero allowances from the independent credit assessment allowance table, would instead be able to also use an independent agency's recommended £ credit limit. Our view is that this would introduce added complexity to the arrangements, reducing the efficiency benefits, and this would also require work to understand the difference between the two forms of assessment and whether adding this new form of assessment would increase risk. We note that the Uniform Network Code (UNC) (for transportation) allows a build-up of payment history allowance over two years and we believe, if A were to be taken forward, alignment of the codes, where possible, helps Suppliers manage their arrangements and it aids efficiency. We also note though that the UNC takes the lower of the independent credit assessment and the credit agency's recommended credit limit. We understand that a DCUSA modification is also consulting on taking this approach. This differs from potential alternative B, which is recommending taking the credit agency's recommended credit limit if the independent credit assessment is zero (i.e. the higher of, in that specific case). We do not feel B is appropriate, particularly if it deviates from the UNC arrangements and the DCUSA proposals by not taking the lower of the two assessments.

Q	Question	Response
8	**What impact do you believe this modification would have on the Consumer?**	We are not able to quantify the impact on the consumer. We do not know what the aggregate value available to Suppliers under independent credit assessments would be when compared to payment history allowance. However, as per Ofgem’s thinking on assessing effective competition, consumers should not be subject to unnecessary costs. If no changes are made to the credit cover arrangements, it is likely that costs will continue to be passed on to consumers through losses caused by insolvencies; on the other side, if the collateral cost associated with the modification increases significantly then that could create issues. On balance, we feel it is fair to remove payment history allowance because a Supplier’s access to (and cost of) other credit arrangements should better reflect its creditworthiness and the risk it imposes on the system. We also feel that consumers would probably be more engaged in the industry if they felt it was working effectively.