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:	*Claire Towler Claire.towler@sse.com*
Company Name:	*SSE Energy Supply 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

Q	Question	Response
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?**	We do not believe that CMP311 better facilitates the CUSC objectives as the proposer has failed to demonstrate that there is a defect in the CUSC credit arrangements, instead they have implied that issues exist in how these arrangements are applied. Therefore, we do not feel that this proposal is justifiable, considering the amount of time, implementation effort and cost involved in this solution. If the proposer's defect is supplier failures, we would like them to note that this solution could trigger further supplier failures, which is an outcome we cannot support. The triggering of supplier failures and the creation of barriers to market entry for suppliers would be a contradiction of Objectives A and B. It is for Ofgem to decide on the standards suppliers need to achieve to operate in the market and not something that can be redefined in an industry code change. We note that Ofgem are currently consulting on proposals to strengthen ongoing requirements on suppliers and arrangements for market exit and consider that this represents the opportunity the proposer seeks to address the defect they have identified.
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 do not support the proposal but, should it progress to implementation, we do support a 12 month implementation period as we believe that is the minimum amount of lead time needed for parties to implement this change. We do however recognise that this solution will have considerable impact on some suppliers, and we cannot speak on their behalf. This consultation should generate responses from the parties that stand to be impacted and they can advise what timeframe they would need to facilitate this change to their credit provision.

3	**Do you have any other comments?**	NGESO has described how its investment grade rating helps it to agree lower cost balancing contracts than would otherwise be the case. Without the rating and the backing of its parent it would be standard practice for many of NGESO's counterparties, including SSE, to reduce the unsecured credit facilities offered. One difficulty we find in this proposal is that Moody's have awarded NGESO the same rating as National Grid plc., yet the basis of NGESO's argument is that their new business model means they can no longer support the amount of credit available to industry. The Proposer says NGESO is uncertain of the reliability of recovering losses from Ofgem; their Credit facility is not guaranteed; the portfolio is more risky than it used to be leading to unpredictable cashflows and is a cause for concern – "no way to run a business". It is difficult to see how the Proposer's arguments do not contradict with the rationale provided by Moody's for their current credit rating. The reasons the rating has been affirmed cannot be the same reasons why the business needs to change in order to protect the rating. If the point of the proposal is to protect NGESO's rating – and this has been stated - there are other more effective approaches available. Further to this, If NGESO is not prepared to remove existing unsecured allowances from a supplier making late payment <u>now</u>, having collateral in place lower than the value of the increasing exposure will not resolve anything. It is understandable that NGESO does not want to carry these debts over 2 or 3 months anymore, but the answer is for NGESO to stop doing this rather than ask other suppliers to fund the practice. The Workgroup recognises this issue is not just with CUSC but is occurring across the networks. Their reluctance to be the cause of or trigger for a supplier to exit the market cannot be a reason to ask all suppliers to provide high-cost collateral. This is inefficient, against best practice and will de-stabilise the sector. The Proposer has said these changes are required because NGESO has changed its business model. Ofgem have recognised NGESO's concerns that it has a different asset base, history and risk profile to other networks. In their most recent RIIO-2 consultation document Ofgem say they have confirmed their price control framework, providing a stable platform for NGESO and incentivising it to deliver positive outcomes for consumers rather focusing on minimising internal costs. In light of the CMA's judgement on the System Operator Northern Ireland, Ofgem's model will remunerate NGESO for the risks it bears including

Q	Question	Response
		cashflow risk related to revenue management activities. They indicate NGESO can extend its current financial facilities to March 2022, including its large revolving credit facility. Moody's when setting the current rating referred to this facility as sufficient to support several years of under-recoveries. Ofgem recommend a working capital facility for what they see as NGESO's continued exposure to revenue collection risk. Ofgem say they have requested further information from NGESO regarding bad debt and this seems an appropriate channel for NGESO to obtain clarity over the debt recovery mechanism. Ofgem confirmed to the Workgroup that the published Best Practice is still valid policy.
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?**	Payment history is one element of credit cover in CUSC, and is the de facto form of credit cover for suppliers entering the market. Its removal risks considerable disruption to new suppliers currently using payment history, and suppliers looking to enter the market in future. This modification would require suppliers entering the market to acquire an independent assessment in order to cover their credit requirements and this may not be possible for all suppliers, thus creating a barrier to entry. We would invite Ofgem to consider whether elements of this proposal create a barrier to entry and hinder competition. It is not in the gift of an industry workgroup to decide the standards that new entrants must meet, this is something for Ofgem to decide as part of the ongoing Supplier Licensing Review. As this proposal obstructs the entry of any new suppliers, we believe the solution is flawed and is not an improvement to current code. It is certainly possible to make changes to code credit arrangements that would truly improve them against CUSC objectives and to the benefit of industry and the consumer. A change that forces the failure of existing suppliers and creates a barrier to entry for new suppliers *may* result in a more robust industry in the long run, but only by dealing significant damage to existing participants. Considering that the Proposer has highlighted the cost of supplier failure as a real difficulty for NGESO, we do not feel it is in any party's interest to approve the current solution.

6	**What impact do you think this modification would have on existing suppliers and what would be the cost to your business?**	We believe this solution would not only prevent new suppliers from entering the market, but it would also trigger the exit of existing suppliers. Removing payment history will cause significant disruption and introduce a sharp learning curve for many suppliers in relation to the different Independent Agencies and Assessments that may *or may not* provide them with alternative and sufficient unsecured allowances. For those suppliers left without sufficient allowances who will be required to secure this credit through other means this is not a small task and could prove very costly. We believe that the intricate nature of this has not been sufficiently illustrated by the Proposer in the Consultation - if anything, it has been deliberately understated. It is appropriate that suppliers should be adequately prepared and follow recognised, responsible risk management practices. Where a Supplier is assessed as less credit worthy it is standard practice that collateral is requested within the trading environment. Within the regulated systems (where the suppliers have no choice of provider) this risk should also be managed but not in a manner that could cause a number of failures simultaneously – this would not be responsible risk management. There is no cost to our business in implementing this change. We do however believe that its effects will cause some suppliers to fail due to being unable to continue operating without sufficient credit cover, which will in turn have costs for industry overall. We would not like this to happen and consider this entirely avoidable. If the Proposer is fully aware that this solution will likely trigger supplier failures and considers it a necessary step to reduce risks in industry, we would urge that wilfully causing supplier failures is not a viable solution. It is in Ofgem's vires to deliberate on the suitability of a supplier to participate in the market, and not something for the workgroup or proposer to decide. If a succession of supplier failures happen as a result of the implementation of this change, it is imperative that we acknowledge that industry, Ofgem, and consumers could justifiably look to the work of this proposal and this workgroup for answers and accountability. Ultimately this proposal has been borne from the proposer's understandable concern about recent supplier failures and the costs associated, and a wish to prevent further SOLRs. Therefore an advisable solution would seek to prevent further events from happening, as

Q	Question	Response
		opposed to broadly trying to remove any supplier seen as a potential liability. It would be preferable to change the system to ensure that if there exists a dependence on good payment history, that this cannot be indefinite, as opposed to changing it so that the option is removed altogether. This would be delivered by the two potential alternatives.
7	**Two potential solutions other than that Proposed have been discussed by the Workgroup, what are your views on these?**	As stated previously, our view on all solutions rests upon our view that a defect has not been demonstrated by the proposer. Supplier failures and the costs associated have been prevalent of late, but the Proposer has not stated how this proposal will address this. The two potential alternative solutions are based on the current CMP311 proposal but add the phasing out of a supplier's usage of payment history. This would give suppliers a mechanism to gain credit cover when they enter the market, with the knowledge that they have to graduate to independent assessment. These alternatives do not include a total removal of payment history, which is the element of CMP311 that we foresee creating supplier failures. We therefore see these proposals as being better designed for the suppliers entering the market, and beneficial for industry as it would ensure that entrants eventually graduate from payment history. Irrespective of which solution is chosen, we would advise awaiting the outcome of Ofgem's Supplier Licence review, which is running concurrently with the development of this change.

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8	**What impact do you believe this modification would have on the Consumer?**	The proposer states that ‘Carrying large unsecured amounts of credit risk may cause the ESO additional financial costs which would need to be recovered from consumers. Establishing more appropriate credit arrangements for all Suppliers would in turn reduce the potential exposure that the ESO carries and ensure that consumers in future are protected from other Supplier failures’ (pg.9), noting that supplier failures result in costs for consumers. Although the point has been raised to them, the proposer has chosen to not comment in this consultation on whether they agree that this change will trigger supplier failures, nor do they comment on the detrimental consumer impact of this. The specific consumer impact section of this consultation is exceedingly brief and hinders our ability to assess this proposal. This section of the consultation states ‘This change proposal should result in beneficial impacts for consumers as the costs of Supplier failure will be covered by appropriate credit facilities as opposed to recovery from consumers in the future’ (pg.12). An industry consultation, especially one that poses tangible financial changes for many in industry, should provide sufficient information for respondents to assess its pros and cons. In this instance the workgroup has failed to produce necessary information on consumer impact. This is despite the point being raised to the proposer in the meetings. This change carries a significant risk of increasing supplier failures, which the proposer acknowledges the consumer is liable to pay for, yet this risk is not articulated in the consumer impact section. This is a detailed and lengthy consultation, and the proposer may understandably be limited in their ability to quantify consumer impact, but this is not justification to deliberately omit it from the consultation. It is true that if carefully designed, thoroughly impact assessed changes were to be made to code credit arrangements, there is potential for consumer benefit. We believe that part of the defect of this modification is the lack of proper impact assessment, and an underestimation of the complexities of code credit.