

## Minutes and Actions Arising from Meeting No.45 Held on 20<sup>th</sup> May 2005 At Brandon Hall Hotel, Brandon, near Coventry

### Present:

Chris Murray	RC	Panel Chairman
Richard Dunn	RD	Panel Secretary
Ben Graff	BG	National Grid Company Representative
Hugh Conway	HC	EnergyWatch Representative
David Edward	DE	Authority Representative
Rupert Judson	RJ	Panel Member
Malcolm Taylor	MT	Panel Member
Bob Brown	BB	Panel Member
Dick Cecil	DC	Alternate Member
Steve Drummond	SD	Panel Member
Steve Phillips	SP	Alternate Member

### In Attendance:

Paul Murphy	PM	NGC
Keith Munday	KM	BizzEnergy
Carl Wilkes	CK	npower
Neil Smith	NS	e.on
Tom Bowcutt	TB	Elexon
Simon Cocks	SC	NGC

## 1 Introductions/Apologies for Absence

255. Apologies for absence were received from Simon Goldring, Paul Jones and David Lane. Dick Cecil was acting as the formal Alternate for David Lane, Steve Phillips was acting as the formal alternate for Simon Goldring and Malcolm Taylor was acting as the formal Alternate for Paul Jones.
256. Chris Murray informed the Panel that he would be moving to the post of Director of Operations and Trading within NGT from 6<sup>th</sup> June and introduced his successor as Director of Commercial, Simon Cocks.

## 2 Minutes of the Meeting held on 22 April 2005

The change-marked minutes of the 44<sup>th</sup> Amendments Panel meeting held on 22<sup>nd</sup> April 2005 circulated on 12<sup>th</sup> May were agreed with no further amendments:

## 3 Review of Actions

257. All the outstanding actions from the previous meeting had been completed or were the subject of agenda items except for the following:

Minute 219 (Definition of Housekeeping). BG confirmed that a definition had been circulated to Panel Members and a number of comments had been incorporated into the Consultation Report for CAP085.

Minute 220 (CAP085 – Revised Treatment of Housekeeping). BG confirmed that it was not possible to change the Amendment Proposal prior to conducting the consultation but NGC would be putting forward a Consultation Alternative Amendment which would address the issues raised in relation to the Authority referring decisions back to the Panel.

Minute 234 (Buy-out of Mandatory Services and Distributed Generation). MT confirmed that he had received papers on these issues and was content with them.

Minute 251 (STC Material). BG confirmed that all those on the CUSC mailing list would receive STC consultation material. This material along with STC Committee papers would also be made available on the STC website.

#### 4 New Amendment Proposals

- **CAPs088 – CAP091**

258. PM gave the Panel a presentation on CAPs088-090. He explained that NGC had put forward CAPs088-090 in order to align the CUSC with the recent Ofgem conclusions document “Best practice guidelines for gas and electricity network operator credit cover”. NGC were recommending that CAPs088-090 should be considered by a Working Group reporting back to the August meeting of the Panel.
259. PM explained that clause 6.6.5 of the CUSC allows for interest to be levied on late payments at base rate +4%. CAP088 would allow for interest to be levied on late payments at a rate equal to the Bank of England base rate + 8% per annum. The rate is set twice a year and is calculated by adding 8% to the reference rate, which is the Bank of England base rate on 30<sup>th</sup> June and 31<sup>st</sup> December each year. The base rate is applicable for the following six month periods i.e. 1<sup>st</sup> July to 31<sup>st</sup> December and 1<sup>st</sup> January to 30<sup>th</sup> June respectively. The change will act as an additional incentive to ensure that payments are made in accordance with prevailing contracts and meets the objective of implementing best practice.
260. PM explained that CUSC currently placed no credit limits within CUSC subject to the party meeting:
- the NGC Credit Rating – A- or A3 respectively as set by Standard and Poor’s or Moody’s for connection charges; or
  - where a Users Licence is issued under the Electricity Act and requires that User to maintain a credit rating, the rating is that as defined in the licence; or
  - Approved Credit Rating – BBB- or Baa3 respectively as set by Standard and Poor’s or Moody’s for Use of System charges

CAP089 would set a maximum credit limit based on 2% of the individual network operator’s Regulatory Asset Value (RAV). The change would provide transparency and consistency across all Network Operators by setting a maximum limit to which subsequent individual user limits can be calculated (as in CAP090 and based on the Basel 2 model) and meet the objective of implementing best practice.

261. PM explained that the CUSC currently set out criteria for obtaining credit (described in Paragraph 260 above). CAP090 would introduce rules for establishing individual user limits based on a percentage of the maximum credit limit. Individual counterparty credit limits and those that use Parent Company Guarantees or aggregates of both should be set using credit ratings applied under the Basel 2 rules for determining bank capital adequacy. An example was provided of the approximate allowances applicable for Standard and Poor's Credit Ratings based on a Maximum credit limit = 2% of RAV (~£120m) as follows:

<b>S&amp;P Credit rating (based on Basel 2 bandings)</b>	<b>Credit allowance as % of maximum credit limit</b>	<b>Approx. Allowance</b>
AAA/AA	100%	£120m
A	40%	£48m
BBB+	20%	£24m
BBB	19%	£22.8m
BBB-	18%	£21.6m

262. KM explained that the CUSC currently made no provisions for the establishment and maintenance of unsecured credit lines for unrated and lower rated companies regardless of credit worthiness. This was having a deleterious effect since unrated and low rated companies did not necessarily present a high risk of default. CAP091 would introduce the establishment and maintenance of an Unsecured Credit Allowance for rated and unrated companies and align the Value at Risk (VAR) calculation with current best practice.

263. Credit Cover best practices involved the establishment of:

- Unsecured Credit Limits
- Value at Risk
- Security of excess VAR over unsecured
- Variety of acceptable tools to provide credit cover
- Monitoring and management of credit exposure
- Appropriate responses to breaches of contract

264. Key elements of CAP091 were the establishment and maintenance of an unsecured credit allowance based on payment record of no less than 0.008% p.a. (escalating monthly) of NGC Regulated Asset Value (RAV) and credit allowances for unrated and lower rated companies based upon annual independent assessment paid for by the NWO and additional assessments paid for by the User.

265. CAP091 also proposed a reassessment of the VAR against best practice guidelines. There was currently over securitisation compared to the actual risks faced by NGC and this also created a barrier to entry. The CUSC was not currently aligned with best practice and in KM's view the current arrangements worked against the CUSC

objective of facilitating competition. CAP091 suggested that an unsecured credit allowance for unrated counterparties could be established by using the payment record, independent assessment would be appropriate for a company which wished to increase its unsecured credit allowance and recalculation of the Demand Reconciliation Credit Cover amount of 10%. In summary KM indicated that the current defects in the CUSC were having an adverse and significant impact on competition now and an expeditious resolution of this problem was required by the end of August 2005. Like NGC's recommendation for CAPs088-090 KM recommended that CAP091 should be considered by a Working Group.

266. In discussion of CAP088 MT noted that the two key changes introduced were to move to a levy of 8% over base rate for late payments compared to a current levy of base rate of 4% over base rate and to introduce the capability to review and revise the base rate at 6 monthly intervals. Several Panel Members believed that 4% over base rate was sufficient incentive already and could not see how moving to 8% over base rate would improve matters given that NGC also made provision for bad debt. PM suggested that 4% was an insufficient incentive to late payers and NGC had evidence that Users were using late payment virtually as a banking facility which strongly suggested the amount was too low. The Ofgem Network Operator best practice guidelines recommended the application of the Commercial Debts (Interest) Act 1998 which referred to 8% over base rate as an appropriate rate to levy on late payers. PM also confirmed that the Distribution NWOs would also be considering the introduction of the terms described under the Commercial Debts (Interest) Act 1998 and the gas industry would be asked to consider a similar amendment to the Unified Network Code (UNC).
267. DC noted that the 8% above base rate indicated in the 1998 Act was optional and not mandatory. He asked if NGC therefore envisaged applying the full 8% above base rate. PM confirmed that this was currently NGC's intention via CAP088 but this should be discussed further by the Working Group. Payment of the new rate would apply equally to NGC as a debtor to other companies in the industry. MT believed that the eventual rate adopted should be a properly incentivising rate rather than excessively penal and should be transparent. He believed that NGC should provide evidence and reasoning to the Working Group to justify the figure it proposed to adopt under CAP088. Panel Members identified a number of other issues that should be considered by any Working Group including a clearer definition of late payment and a clearer definition of base rate.
268. In discussion of CAP089 SD and DC were concerned at the lack of detail provided in the Amendment Proposal concerning the impact on the CUSC. Both believed that the issue might have been better discussed by a Standing Group as there were a range of criteria that could be adopted to identify a maximum credit limit. BG explained that NGC had been deliberately high level about the impact on the CUSC since it recognised that this was a complex area and wanted to work with the Industry to develop refined solutions via a Working Group. MT agreed with DC's and SD's concerns over the level of the information provided on the impact on the CUSC but agreed that a Working Group should be established to consider all the credit related Amendment Proposals with the onus on NGC to develop its case in the Working Group on a number of detailed issues including a maximum credit limit based on 2% of RAV. BB and SD agreed with MT's comments.
269. On CAP090 MT asked if the main consideration of the Working Group would be which final figures to put forward in the table of figures covering credit allowance, credit allowance as a % of maximum credit limit and approximate allowance. PM

confirmed that this was the case. DC note that CAP090 could be capable of quicker resolution than the other credit related proposals. BG confirmed that, subject to discussions in the Working Group, it might be possible to report back to the Panel in quicker timescales on some of the Amendment Proposals and NGC would encourage the Working Group to do this.

270. On CAP091 KM indicated that the Demand Reconciliation Credit Cover amount of 10% was too high. PM indicated that companies consistently under-forecast and this had been recognised in CAP055 which had been approved by the Authority. PM therefore believed that 10% was appropriate. MT was concerned that the Working Group should have some guidelines to consider any recalculation of the 10% figure. JG suggested that historic analysis produced by the Electricity Pool could be revisited by the Working Group to see how demand charges had changed.
271. The Panel AGREED that CAPs088-CAP091 should be considered by a Working Group chaired by Ben Graff of NGC. The Panel AGREED the Membership of the Working Group (subject to several confirmations) and draft Terms of Reference (TORs). The Working Group would refine the TORs at its first meeting and submit them for approval to the June Panel meeting. It was AGREED that the Chairman should make a verbal report to the Panel in June and July on the Working Group's progress. The Working Group's final Report should be submitted to the August Panel Meeting although if the Working Group completes its deliberations on any Amendment Proposal earlier than this the Group should report accordingly to the Panel.

**Action: BG**

272. MT noted that there could be consequential changes to NGC's charging methodology arising from CAPs088-091. MT also noted that NGC's business would be less risky if these credit related Amendment Proposals were implemented and asked if Ofgem would reflect this in due course in NGC's allowable rate of return. DE indicated that Ofgem would consider these issues in the round as part of setting the next price control for NGC.

## 5 Standing/ Working Group Reports

- **Balancing Services Standing Group**

273. JG gave the Panel a report on the work of the Group since the last Panel meeting. The Group had met once since the April Panel meeting and most of the time was spent on considering implementation issues associated with CAP047 (Competitive Process for Mandatory Frequency Response) due to be introduced on 1<sup>st</sup> October 2005. NGC had discretion on certain issues such as publications explaining the new process but were keen to reach consensus on such issues in the BSSG. JG would report back to the June Panel meeting further on this issue and it would also be discussed at the June meeting of the Operational Forum.
274. On buy-out useful discussions had been held on what was proving a difficult subject. NGC would provide a paper to a future meeting attempting to define the scope of the services that could be subject to buy-out. The main six-monthly report from the BSSG would be provided to the July Panel meeting at which time the Panel would be invited to extend the Terms of Reference for the BSSG for another six months.

### 6 Consultation Reports

- **CAP085 – Revised Treatment of Housekeeping Amendments**

275. The Panel NOTED that the consultation on CAP085 would close on 25<sup>th</sup> May.

- **CAP086 – Proposal for Earlier Consideration of Implementation Dates**

276. The Panel NOTED that the consultation on CAP086 would close on 27<sup>th</sup> May.

- **CAP087 – Revisions to Request for Urgency Process**

277. The Panel NOTED that the consultation on CAP087 would close on 1<sup>st</sup> June.

### 7 Amendment Reports

- **CAPs079 – 084 – Housekeeping Amendments**

278. The Panel NOTED that this Amendment Report had been provided to the Authority on 4<sup>th</sup> May.

### 8 Authority Decisions

279. There were no new Authority Decisions.

### 9 Appeals Against Code Decisions under the Energy Act 2004 and the subsequent Order

280. BG referred to MAY-05-02 – Note by NGC previously circulated to Panel Members. He explained that the DTI consultation exercise on this issue was expected to conclude shortly with the publication of its conclusions document and the laying of an Order before Parliament providing details of the appeals arrangements under specific Codes. It was expected that the CUSC would be one of the designated Codes in the Order.

281. BG explained that MAY-05-02 outlined two possible options for ensuring that Panel Member Recommendations are included in CUSC Amendment Reports. The first focused on ensuring that the Panel reaches a collective view at the draft Amendment Report phase. NGC would highlight the need for a Panel recommendation at Panel meetings and seek views on whether a conference call or “face to face” meeting was required. In the case of non-contentious Proposals e-mailing of Panel Members’ views could be employed. The Panel view would then be incorporated into the draft Amendment Report with NGC suggesting a time and date for the Panel to discuss its recommendation. The Amendment Report would then be circulated to Panel Members again (incorporating the Panel’s recommendation) just before it was submitted to Ofgem. The second option focused on Panel Members providing an independent recommendation at the consultation phase. Panel Members would be prompted to indicate if they believed the Amendment Proposal (or any Working Group Alternative Amendment) better facilitated the Applicable CUSC objectives.

The process would be repeated in the event of any Consultation Alternative Amendments. Panel Members' decisions would then be recorded in the Amendment Report and their reasons for those decisions.

282. SD indicated that he had spoken with the DTI that morning and also understood that there would be a delay in laying the Order before Parliament. The Order would be subject to negative resolution of the House and would need to be laid for about three weeks. He also expected the CUSC to be a designated Code under the Order. He did not believe that the Panel would need to provide its views under the Order until July and agreed with the proposals in MAY-05-02 that a work-around solution was appropriate until then. He suggested that the Governance Standing Group should be reconvened to consider the issues once the DTI conclusions paper was available and the Order had passed through Parliament.
283. During discussion of MAY-05-02 DC indicated that he preferred option 1 since collective discussion by the Panel would be valuable to assist all Panel Members to reach a view. Panel Members also noted the written comments submitted in advance of the meeting. SD expressed some concerns about the logistics of the tight timetables for obtaining Panel Members' views implied by option 1. However, Panel Members' generally confirmed that option 1 was preferable as a short term approach to the issue and considered that the Governance Standing Group should assess the need for a more formal amendment after the DTI conclusions were published and the Order in force. BG agreed to bring back more detailed options for decision at the next Panel meeting.

**Action: BG**

### **10 CUSC Panel Elections**

284. The Panel Secretary referred to MAY-05-01 - Note by NGC on the arrangements for the 2005 Amendments Panel Elections. He confirmed that the election process would commence at the end of June with requests to CUSC Parties for nominations for Panel Members and the timetable would then proceed as described in MAY-05-01. The Panel NOTED these arrangements.
285. In response to a question from SP, BG confirmed that Dormant CUSC Parties were entitled to vote in the forthcoming elections since they were Parties to the CUSC Framework Agreement. He agreed that the report on the election which NGC would provide to Ofgem in the Autumn of 2005 would refer to voting by Dormant Parties.

**Action: BG**

286. The Panel Secretary requested any comments from Panel Members on the draft User Guide previously provided no later than 31<sup>st</sup> May so that this could be circulated to CUSC Parties in early June.

**Action: Panel Members**

### **11 Report on Other Industry Documents**

287. MT reported that the BSC Panel met on 12<sup>th</sup> May and Members were introduced to Stuart Senior, the new Chief Executive of Elexon. He noted that Ofgem had rejected P157 (Charges on Suppliers). P157 contained a variety of different elements not all of which Ofgem could approve and therefore it had to be rejected. This was a further indication that Amendment Proposals for the CUSC needed to be fairly narrowly

defined to ensure that they were not rejected.

288. BG indicated that the STC Committee would meet again on 25<sup>th</sup> May. The main topic for discussion would be incorporating the provisions of CAP068 (Competing Requests for TEC) in to the STC.

### **12 Any Other Business**

289. The Chairman thanked the Panel for their constructive approach to business and for the quality and good nature of the debates during his tenure as Panel chairman. He wished the Panel well in the future.

### **13 Record of Decisions – Headline Reporting**

290. The Panel Secretary would circulate an outline Headline Report after the meeting and place it on the National Grid website in due course.

### **14 Date of Next Meeting**

291. The next meeting will be held on Friday 24<sup>th</sup> June 2005 at the Brandon Hall Hotel, Brandon, near Coventry commencing at 10.30am.