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<b>Paper Reference:</b>	<b>SECP_69_1406_12</b>
<b>Action:</b>	<b>For Decision</b>

## DP076 Problem Statement

### 1. Purpose

Draft Proposal [DP076 'Pursuing Non-Payment in Events of Default'](#) was raised by British Gas and the Development Stage of the proposal has concluded. The Change Sub-Committee believe this Draft Proposal is ready to be converted to a Modification Proposal. This paper sets out our proposed approach for progressing this modification for the Panel's approval. We are recommending that this modification be progressed to the Refinement Process, and that the Panel agree the package of work to be undertaken.

This paper provides a high-level summary of the key points. A copy of the problem statement submitted by the Proposer can be found in Appendix A.

### 2. Summary of the issue

#### What is the issue?

The wording of SEC Section J2.6 means that the Data Communications Company (DCC) will keep the Panel updated on matters regarding pursuing non-payment, as well as allowing the Panel to express their views, but ultimately the DCC must decide what they consider to be the best course of action (unless the Panel say it is no longer worthwhile trying to recover the costs). This approach puts the DCC at risk as they decide how to comply with the obligation, and also need to justify their approach for the purposes of price control. This could lead to an increased risk of costs to be socialised if action is not taken swiftly enough.

#### What is the proposed solution?

The Proposer had anticipated that this modification would proceed to the Report Phase and had provided some draft legal text to assist, which is provided in Appendix B. This legal text sought to address this issue by amending Section J2.6(b) to oblige the DCC to follow any instructions given by the Panel in the pursuit of non-payment, rather than consult with the Panel under the current arrangements.

### 3. Proposed progression

The Change Sub-Committee have agreed that this Draft Proposal is ready to be converted to a Modification Proposal. We believe that this modification should be progressed to the Refinement

Process to allow for an assessment of the Proposer's proposed solution to the issue. This is due to the points raised by the Change Sub-Committee, who were not sure that the proposed solution would meet the Proposer's intent. The DCC also raised some comments on the proposed solution and believed that the proposal would benefit from the Refinement Process, which the Change Sub-Committee agreed with.

### Work package and timetable

We propose the following package of work to be undertaken during the Refinement Process:

Activity	Date
Discuss at the July Working Group meeting	03 Jul 19
Refinement Consultation	05 Jul 19 – 26 Jul 19
Modification Report considered by Panel	09 Aug 19

### Areas of assessment

As part of the assessment of this modification's solution, we believe the following questions need to be answered in addition to the standard assessment areas.

### *Who should have authority over matters regarding the pursuit of non-payment?*

The Change Sub-Committee noted the comments raised by the DCC who understand the intentions of this proposal and the types of issues it is trying to mitigate. However, they were concerned with the proposed solution as they felt it could unintentionally pose a conflict of interest. Noting this, the Change Sub-Committee agreed that the proposed solution would benefit from the Refinement Process.

## 4. Recommendations

The Panel are requested to:

- **AGREE** that DP076 is ready to be converted to a Modification Proposal;
- **AGREE** that MP076 should be progressed to the Refinement Process; and
- **AGREE** the package of work and the timetable for MP076.

Joe Hehir

SECAS Team

7 June 2019

### Attachments:

- **Appendix A:** DP076 problem statement
- **Appendix B:** DP076 draft legal text

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# DP076 ‘Pursuing Non-Payment in Events of Default’

## Problem statement – version 0.3

### About this document

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This document provides a summary of this Draft Proposal, including the issue or problem identified, the impacts this is having, and the context of this issue within the Smart Energy Code (SEC).

### Proposer

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This Draft Proposal has been raised by Simon Trivella from British Gas.

## What is the issue or problem identified?

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### Background

The number of Events of Defaults handled by Smart Energy Code Administrator and Secretariat (SECAS) increased in the last financial year (2018/19). Most Events of Default are due to non-payment of Data Communications Company (DCC) Charges, and in many cases the company ceased trading; nine Parties exited the Smart Energy Code (SEC) in the last financial year. If a company ceases trading and has outstanding payments which cannot be paid by Credit Cover, costs will be socialised amongst SEC Parties.

One Event of Default saw a Party unable to pay its DCC Charges in November 2018. They admitted that payment would not be possible for the next four months and the Party went on to remain in an Event of Default for five months. Whilst payment was eventually recovered through the creation and commitment of a repayment plan, there was a tangible possibility that whilst outstanding payment was accruing, there was potential for a greater cost to be socialised amongst SEC Parties. Due to the wording of Section J2.6, the DCC were obliged to consult with the Panel over pursuing the non-payments in the Event of Default, but it did not require the DCC to follow the Panel's instructions on the course of action to be followed.

### How does this issue relate to the SEC?

Section J2.6 of the SEC addresses payment default. It currently states that the DCC must notify the SEC Panel of a payment default, and that the DCC shall 'take all reasonable steps and proceedings to pursue payment'.

There is a general concern that the way that payment defaults are currently handled could affect the outcome of future defaults, and the SEC Panel propose to eliminate the possibility for SEC Parties to pay socialised costs as far as possible.

The DCC currently seek to pursue payment and consult with the SEC Panel, and the SEC Panel would like to address the ambiguity surrounding who has authority on the matter.

## What is the impact this is having?

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### What are the impacts of doing nothing?

In practice the wording of Section J2.6 means that the DCC will keep the Panel updated on matters regarding pursuing non-payment as well as allowing the Panel to express their views, but ultimately the DCC must decide what it considers to be the best course of action (unless the Panel say it is no longer worthwhile to try and recover the costs). This approach puts the DCC at risk by deciding how to comply with the obligation, and in terms of justifying its approach for the purposes of the price control, which could increase the risk of increased costs to be socialised if action is not swift enough.

For the avoidance of doubt, if the DCC does not take all reasonable steps and proceedings to pursue and recover debts, the DCC will be in breach of the SEC and therefore in breach of its licence and at risk of Ofgem taking enforcement action. This may mean the DCC are unable to pass-through the bad debt under its price control. The Panel should notify Ofgem if the Panel considers that the DCC is in breach of Section J2.6 so that Ofgem can consider enforcement action, and so that Ofgem can decide whether to ultimately allow some, all or none of the bad debt under the DCC's price control.

## What are the views of the industry?

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### Views of the DCC

The DCC provided some points for consideration under the issue raised by the Proposer, noting that these don't necessarily impact the SEC wording itself:

- How should the DCC receive its instructions to act in an Event of Default?
- How should the appeal mechanism would work? Would the organisation subject to the Event of Default appeal to Ofgem or the Panel and what would be the timescales involved?
- Should the DCC only act in an Event of Default once they receive instructions to undertake any reasonable steps?
- Should 'reasonable steps and proceedings' be defined?

These points were noted by the Change Sub-Committee who agreed that they would not have a direct impact on the SEC itself.

### Views of SEC Parties

No comments were received from other Parties during the Development Stage.

### Views of the Change Sub-Committee

The Change Sub-Committee discussed this proposal at their meeting on 28 May 2019 where they agreed that the issue is clearly defined and understood.

The DCC understood the intentions of the proposal and the types of issues it was trying to mitigate. However, they were concerned with the proposed solution as it was their view that a singular group made up of SEC Parties could unintentionally cause a conflict of interest by managing bilateral transactions between the DCC and SEC Parties. The DCC considered that the current arrangements were more suitable as it meant an impartial Party would manage such matters.

There was discussion regarding the process of pursuing non-payment, and whether larger Parties should be held responsible if smaller Parties cannot pay their debt. The Authority confirmed that price control methods are used to acquire the debt. They also noted the importance of Ofgem and the DCC ensuring that the process is suitable for each case. The Authority considered, and the Change Sub-Committee agreed that the proposal would benefit from the Refinement Process in order to give Parties the opportunity to provide comment and feedback on the solution.

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# DP076 ‘Pursuing Non-Payment in Events of Default’

## Legal text – version 0.1

### About this document

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This document contains the redlined changes to the SEC that would be required to deliver this Modification Proposal.

These changes have been drafted against SEC Version 6.12.

## Section J 'Charges'

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**Amend Section J2.6 as follows:**

### **J2     PAYMENT DEFAULT AND DISPUTES**

#### **Notification of Payment Failure**

J2.1     Where a Party fails to pay an amount set out in an Invoice by the relevant Due Date, then the DCC shall, on the Working Day following the Due Date, issue a notice to that Party:

- (a)     setting out the unpaid amount; and
- (b)     referring to the matters set out in Sections J2.2, J2.4, J2.5, J3.16 (where applicable), and M8.1(c) (Events of Default).

#### **Default Interest**

J2.2     Where a Party fails to pay an amount set out in an Invoice by the relevant Due Date, then that Party shall pay interest on that amount at the Default Interest Rate calculated from day-to-day from the Due Date to (but excluding) the date on which payment is made (compounded monthly).

#### **Notification of Payment Disputes**

J2.3     Where a Party wishes to dispute any amount set out in an Invoice addressed to it, then that Party shall nevertheless pay the full amount set out in the Invoice by the Due Date, and shall give notice to the DCC of the disputed amount and the reason for the dispute. A Party may not give notice under this Section J2.3 (or otherwise dispute an amount set out in an Invoice) more than 12 months after the Due Date for that Invoice.

#### **Resolution of Payment Disputes**

J2.4     Where a Party disputes, in accordance with Section J2.3, any amount set out in an Invoice addressed to it, then:



- (a) such Party and the DCC shall each in good faith negotiate to resolve the dispute amicably and as soon as reasonably practicable after it arises;
- (b) the DCC shall provide all such evidence in support of its position as the disputing Party may reasonably request, and the DCC shall provide such evidence within 5 Working Days after such request;
- (c) no earlier than 1 Working Day after receipt from the DCC of the information requested under Section J2.4(b) (or, where the DCC does not comply with such request, on the expiry of the period referred to in that Section), the disputing Party may refer the dispute to the Panel, in which case each of the DCC and the disputing Party shall be entitled to provide written submissions in support of its position;
- (d) where a dispute is referred to the Panel in accordance with Section J2.4(c), the Panel shall convene a meeting and determine the dispute within 10 Working Days of the reference being made (to which meeting representatives of the disputing Party and the DCC may be invited in accordance with Section C (Governance)); and
- (e) where the Panel determines that there has been an overpayment to the DCC, the DCC shall include an adjustment in accordance with Section J1.9(c) to address such overpayment (or comply with any direction of the Panel to repay the relevant amount together with interest at the rate that would have applied had the adjustment been made in accordance with Section J1.9(c)).

J2.5 Section J2.4, and any determination by the Panel pursuant thereto, are without prejudice to the following rights of the Parties:

- (a) where the amount set out in an Invoice addressed to a Party is disputed on the grounds of whether or not the Charges were calculated and levied in accordance with the Charging Methodology and the Charging Statement, then either of that Party or the DCC may refer the matter to the Authority for determination pursuant to Condition 20 of the DCC Licence; or

- (b) where the amount set out in an Invoice addressed to a Party is disputed on any other grounds, then either of that Party or the DCC may refer the matter to arbitration in accordance with Section M7 (Dispute Resolution).

### **Pursuing Non-Payment**

J2.6 Where the DCC has served a notice in accordance with Section J2.1 in respect of Charges payable by a Party, and such Charges have not been paid within three (3) Working Days following that notice, the DCC shall:

- (a) as required by Section M8.2 (Notification of Events of Default), notify the Panel that an Event of Default has occurred in respect of that Party under Section M8.1(c); and
- (b) the DCC shall take all reasonable steps and proceedings (in ~~consultation~~ with accordance with any and all instructions given by the Panel) to pursue and recover the unpaid amount (together with interest), and shall continue with such steps and proceedings unless and until the Panel (whether on the application of the DCC or otherwise) determines that it would not be worthwhile to do so in the circumstances (having regard to, amongst other things, the DCC's duties under part D of Condition 11 of the DCC Licence).

J2.7 Any Party may appeal the decision of the Panel under Section J2.6 to the Authority, and the DCC shall comply with any decision of the Authority in respect of such matter (which shall be final and binding, but without prejudice to the Panel's ability to make a further decision under Section J2.6 following a material change in circumstances).

### **Records**

J2.8 Without prejudice to any other requirements under Laws or Directives, the DCC shall maintain records of each Invoice (together with reasonable supporting evidence for the Charges levied in the Invoice) for a period of at least 18 months following the date of the Invoice.