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DP095 ‘Alignment of SEC Credit Cover’

Problem statement – version 0.1

About this document

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

This Draft Proposal has been raised by Ashley Pocock from EDF Energy.

What is the issue or problem identified?

In the financial years 2018/2019, and 2019/20, five SEC Parties ceased trading, and it is anticipated that more will follow. This has so far resulted in unpaid DCC charges of c£731,000 being socialised amongst all other SEC Parties. Of the five parties ceasing to trade, the credit cover circumstances have varied. The most significant example is where a SEC Party had sufficient credit cover for the first month's missed payment, but not for the following months. This alone resulted in c£362,000 being socialised amongst all SEC Parties.

To mitigate the risk of costs being socialised and affecting other SEC Parties, the SEC contains Credit Cover requirements. Credit cover is calculated and held by the DCC in the event that a SEC Party is unable to pay their monthly charge. Credit cover is intended to avoid unpaid charges from being socialised and it is important that all SEC Parties adhere to the credit cover requirements to minimise the impact should they enter into an Event of Default.

However, to date the current arrangements have not prevented the costs of defaulting Parties from being socialised.

The Proposer therefore wishes to explore the current credit cover requirements to identify if there are ways it can be amended to reduce the risk of cost socialisation across the industry.

As part of this modification, other aspects surrounding the Defaults process will also be explored, such as actions which the SEC Panel can take when a default occurs or is anticipated, and the actions of and escalations to the Authority.

It will also look at other Codes in order to identify opportunities for best practice and consistency as was considered previously in SECMP0016. Modification [SECMP0016 'Consideration of Maximum Credit Value in Credit Cover Calculation'](#) reduced the total amount of Credit Support that Parties are required to lodge with the DCC, enabling more Parties to become SEC Party members. In recent months however we have seen an increased frequency in Events of Default.

How does this issue relate to the SEC?

Currently, the SEC credit cover requirements feature a complicated calculation to ascertain the level of cover a Party must have in place. Due to the parameters of the credit cover calculation set out by the SEC, not all Parties must lodge for credit cover. This has resulted in high costs being socialised amongst other SEC Parties in the unfortunate event of a default.

In the event of a default, the Panel are able to take certain actions themselves including the revocation of the following rights, as stated in SEC Section M8.5:

- (a) the right of the Defaulting Party (and each other member of its Voting Group) to vote in Panel Member elections under Section C4 (Panel Elections);
- (b) the right of the Defaulting Party to raise new Draft Proposals under Section D (Modifications); and
- (c) the right of the Defaulting Party to influence the appointment of a Change Board Member, so that:
 - (i) in the case of a Supplier Party, the Change Board Member appointed by the Voting Group of which that Supplier Party forms part shall be suspended; or

- (ii) in the case of any Party other than a Supplier Party, the Secretariat shall ignore the views of that Party when considering any request to appoint or remove a Change Board Member appointed by the Party Category of which that Party forms part.

Further actions require approval of the Authority (Ofgem). It has been noted that the process of gaining approval can be drawn out, and it has been suggested that an expedited process may reduce the risk of costs being socialised. Withdrawing certain rights from a defaulting Party should, in theory, provide incentive for them to take action in resolving the Event of Default in order to reinstate their rights as quickly as possible.

SEC Section M8.6 states that in the event of a default, the Panel must request authorisation from Ofgem to withdraw:

- (d) the right of the Defaulting Party to receive Core Communication Services or Local Command Services in the 'Other User' User Role;
- (e) the right of the Defaulting Party to receive Core Communication Services or Local Command Services in any User Role other than the 'Other User' User Role;
- (f) the right of the Defaulting Party to receive any or all Elective Communication Services;
- (g) the right of the Defaulting Party to initiate Enrolment of Smart Metering Systems; and
- (h) the right of the Defaulting Party to request or receive any or all Services other than those referred to elsewhere in this Section M8.6.

Under these circumstances, SECAS will aim to build a case to suggest that Ofgem should approve the Panel's decision to suspend these rights.

In order to gain Ofgem's approval as quickly and as efficiently as possible, we propose to explore options in conjunction with the other energy industry codes. A potential collaboration with an existing code could accelerate an approval, as the event of default could prove more urgent.

What is the impact this is having?

If a Party ceases to trade and they do not have sufficient credit cover, or it was not deemed necessary for them to have it, all costs are socialised amongst SEC Parties. This has occurred twice in the past financial year and is creating frustration amongst SEC Parties that a more effective system has not yet been implemented.

If left as is, there could be many more examples in the future where Parties ceasing to trade or behaving in a manner which leads to default result in having their unpaid charges socialised.

What are the views of the industry?

Views of the DCC

The views of Parties will be gathered during the Development Stage.

Views of SEC Parties

The views of Parties will be gathered during the Development Stage.

Views of Panel Sub-Committees

The views of Panel Sub-Committees will be gathered during the Development Stage.

Views of the Change Sub-Committee

The views of the Change Sub-Committee will be gathered during the Development Stage.