

UNC Review Group 0252
Review of Network Operator Credit Arrangements
- Strawman options for discussion on payment history

1. Introduction

Review Group 0252 (RG0252) was established in July 2009 to allow a review of the existing arrangements within UNC TPD Section V and to take account of other credit related issues that have occurred since the publication of the Best Practice Guidelines (BPG) document.

This strawman defines potential options for changing the way Payment History is accrued, which National Grid believes should be discussed further as part of the scope of RG0252:

- Option A – UNC ASIS but clarifying current text
- Option B – CUSC Variation
- Option C – Alternate/Wider Payment History Options

2. Payment History Options

The current UNC Payment History requirements are detailed in V3.1.5 and V3.1.6, these arrangements allow for payment history to be built up over a 5 year period, however when a payment of greater than £250 is late then the accumulated history would be taken back to zero.

Option A – UNC ASIS but clarifying current text

National Grid believes that payment history as detailed in UNC has caused some confusion, for example one User thought credit Payment History only applied after 12 months and it may be worth the Review Group considering if the current text could be clarified to ensure all UNC parties understand how the process works.

UNC (currently)

- 3.1.5 The Transporter may allocate an Unsecured Credit Limit to a User based upon the period of time elapsed that such User has paid all invoices by their due date for payment in accordance with Section S, such that after a calendar month, a User may be allocated an Unsecured Credit Limit on the basis of 0.4% of the relevant Transporter's Maximum Unsecured Credit Limit over a 12 Month period and increasing on an evenly graduated basis each Month up to a maximum of 2% of the relevant Transporter's Maximum Credit Limit after 5 Years.
- 3.1.6 Where a User has been allocated an Unsecured Credit Limit pursuant to 3.1.5 above, and such User subsequently fails to make payment in full of any invoice (other than in respect of Energy Balancing Charges) issued in accordance with Section S:

- a) with a total amount due of £250 or less, then such User's Unsecured Credit Limit shall be reduced by 50% from the date of such payment default; or
- b) with a total amount due of greater than £250, or where a User fails to make payment on any other occasion within 12 Months of a default as set out in (a) above, then such User's Unsecured Credit Limit shall be reduced to zero from the date of such payment default.

The User's payment history may continue to be used following the date of any payment default as set out above to increase the reduced value of the User's Unsecured Credit Limit in accordance with paragraph 3.1.5 above.

Option B – CUSC Variation

It has been suggested that the current UNC rules (V3.1.6) with regards to reducing the code credit limit (allocated through payment history) to the position of zero for late payment may be considered extreme, particularly if the User has accumulated a considerable period of payment history. It may be worth noting that Ofgem's implementation letter for UNC 0026 'Application of Charges consistent with Late Payment of Commercial Debts (Interest) Act 1998' states:

- *Ofgem is of the opinion that all parties should make arrangements to meet their obligations in a timely manner. Where this does not occur in relation to payment terms, Ofgem believes that a number of remedies, including interest and administration charges, should be applied.such charges should not be extreme or excessive.*

With this in mind, National Grid suggests that the Review Group may wish to discuss the CUSC methodology option which broadly is:

- Case 1 - User pays on time: User's payment history allowance increases (providing all other invoices are paid on the due date in that month) as with the UNC by 0.0006 to a maximum of 2% of 2% of RAV;
- Case 2 - User pays up to (and inc.) 2 days late: User's payment history all remains as it is with no increase (providing all other invoices are paid within 2 days of the due date in that month);
- Case 3 – User pays more than 2 days late: User's payment history allowance decreases. A stepped reduction is carried out under the CUSC, whereby there's a 50% reduction in allowed credit upon the 1st missed payment and a 100% reduction upon the 2nd such late payment within a rolling 12 months.

Under the CUSC model there would still be an advantage for the user paying on time as their code credit limit would increase. There is no minor error threshold (£250) in the CUSC model, the argument for not having the UNC £250 limit is that it is in fact easier to

make a 1 digit typo (£100, £1000, £1m, etc.) than it is to make a 2 digit typo (which £250 would be). *[Does anyone know the rationale for the £250 amount?]*

We believe that a variation on the CUSC model could be adopted into the UNC as follows:

- A User will continue to be allocated an Unsecured Credit Limit on the basis of 0.4% of the relevant Transporter's Maximum Unsecured Credit Limit over a 12 Month period and increasing on an evenly graduated basis each Month up to a maximum of 2% of the relevant Transporter's Maximum Credit Limit after 5 Years.
- The UNC £250 minor error element and reductions in payment history will be removed.
- The following CUSC (like) elements will be adopted instead:
 - The first time a late payment occurs, provided it is no later than [2] days the payment history is retained but no increase in payment history is accrued for that month.
 - The second time a User pays late (no later than [2] days) within a rolling 12 months of the first missed payment then a stepped reduction of 50% is made.
 - The third time a late payment is made (no later than [2] days) within a rolling 12 months of the first missed payment, then a 100% reduction is made.
- With regards to the [2] days 'grace' interest charges and all other sanctions per Section S3.5 would still apply.
- For the avoidance of doubt any payment received after 2 days would result in the payment history reverting to zero.

It is important to note this is a variation on the CUSC model. In the CUSC as long as the User Pays within the 2 days grace period they do not have a reduction on their Payment History Credit limit and the only 'penalty' for late payment within 2 days is the lack of increase in the Payment History credit limit for the following month. This variation introduces a "3 strikes" rule, which we believe is less extreme than the current UNC text.

We would welcome discussion on this option, in particular whether this option is more complex resulting in more operational costs. Views are also sought on the [2] days grace, (as to whether this should be included) and the number of "strikes" (late payments) allowed before the payment history is reduced to zero..

Option C - Alternate/Wider Payment History Options

As a consequence of conducting the analysis related to the aforementioned Payment History options, National Grid consider there is merit in reviewing the principal of Payment History. The drivers behind this view are:

- The use of payment history is a rare event, with only one (National Grid) User currently obtaining an Unsecured Credit Limit via this route.
- Review Group 252 has been looking to improve the transparency and clarity with regards to Independent Assessment. It is our view that this revised process is the most appropriate method to allocate Unsecured Credit to smaller UNC parties.

- The independent Assessment also takes into consideration payment history (both to the GT and other parties) when determining the final score/amount of Unsecured Credit to be provided.

The two options below have been developed as a means of generating discussion in this area and National Grid acknowledge that there could be other options worthy of evaluation.

1. **Remove the option of Payment History from UNC.** As payment history as a credit tool has currently had very limited usage, we do not believe such an action would be to the detriment of Users.
2. **Restrict payment history to new Users only.** If removal of payment history was thought to be a step too far, we believe there is merit in restricting its use to new Users.
 - We also believe the **time period** Users can increase their Code Credit limit should also be limited to a fixed period of time [24 months] from start up date. .After the end of the [24 months] period the User would provide an alternative credit arrangement such as Independent Assessment.
 - **The amount of code credit cover**
 - a. could be based on the **same basis as now** (0.4% of the relevant Transporter's Maximum Unsecured Credit Limit per 12 Month of payment history). However, as the period has been reduced (from 5 years), the maximum level of Code Credit that could be acquired would be reduced.
 - b. it has been suggested that a simpler approach could be taken where an amount (maximum value/[24]) could be released for every month good payment history is maintained up to a **maximum cash value** [£300,000?]. If a late payment occurs either the current UNC rules or the CUSC principles could apply (see option A & B for details)
 - c. If the Review Group determines that linking Unsecured Credit levels to RAV (as per existing provisions) remains appropriate, **reduce the %** that can be accumulated. Currently Users can accrue up to 2% of the maximum level (2% of Transporter's RAV). Consideration could be given to reducing this to [1% or 0.5% etc]? This will reduce the absolute £ risk but will not be a departure from Unsecured Credit linkage to RAV.

Conclusion

National Grid raises these as items for the Review Group to discuss and welcome input and opinions on them.