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## P426 Workgroup 1 Summary

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### Summary

#### 1 Welcome and Meeting Objectives

The Chair welcomed attendees and presented the following meeting objectives to Workgroup Members:

- Consideration of the background to P426 and proposed solution
- Consideration of the P426 Terms of Reference

#### 2 What is the issue and proposed solution?

- 2.1 The Proposer, Drax Energy Solutions Limited, explained that as Energy Indebtedness is calculated individually for each BSC Party and Credit Cover must be lodged on that basis, there is no option for Suppliers within the same group to provide collective credit arrangements, which can result in disproportionate and inefficient levels of credit being lodged in aggregate.
- 2.2 The proposed solution is to provide the option that related BSC Parties are able to rely on shared credit arrangements and provision. Energy Indebtedness of each related BSC Party should be combined and the Credit Cover Calculation then performed on the combined position.
- 2.3 The Proposer believes that this will better facilitate Applicable BSC Objectives (c) (effective competition) and (d) (efficiency in the balancing and settlement arrangements) when compared to the current baseline.
- 2.4 A Workgroup Member asked what the Proposer means by “within the same group” and the Proposer replied that this would be explored in the discussion. The Workgroup Member explained that there is a reason why the current credit arrangements are structured as they are as a BSC Party is linked to a company with limited liabilities, would the banks be happy with the proposed arrangements? If there was to be a Parent Company Guarantee (PCG) arrangement then this approach had already been debunked by previous issues with Enron and TXU.
- 2.5 A Workgroup Member explained that it would be incumbent on the Workgroup and the Proposer to develop quantitative and/or qualitative evidence of a potential reduction in credit collateral lodged overall versus the cost of implementing the proposed solution.
- 2.6 The Workgroup discussed which types of organisations could benefit from the proposed solution and it was felt there were a number of different types based on representation on the Workgroup, not just large vertically and/or horizontally integrated companies.

#### 3 Terms of Reference

- 3.1 Elexon presented the P426 Specific and Standard Terms of Reference as agreed by the Panel.
- 3.2 The Proposer and Workgroup will need to consider all of the Terms of Reference as part of the P426 Assessment Procedure.

#### 4 Overview of BSC Credit Cover arrangements

- 4.1 Elexon provided an overview of the BSC Credit Cover arrangements.
- 4.2 A Workgroup Member asked if the Credit Default and Payment Default processes can be explained as they felt it was relevant to the discussion and for the Workgroup to understand. Elexon agreed to provide an overview at the next Workgroup meeting.
- 4.3 A Workgroup Member asked why the Credit Assessment Price (CAP) is used in the Credit Cover calculation rather than actual imbalance prices. A Workgroup Member explained that actual imbalance prices are not available until the Interim Information (II) Settlement Run (Settlement Date +5 Working Days).
- 4.4 Elexon mentioned that an Issue Group on Credit is due to be formed and this will discuss Credit Cover arrangements. The Proposer explained that they were happy with the current minutiae of the arrangements, so this is not in the scope of P426, but want to be able to net across Parties.

## 5 Benefits of the proposed solution

- 5.1 The Proposer explained the benefits of the proposed solution, using some worked examples to demonstrate the reduction in the amount of collateral that will need to be provided without impacting on credit risk and that the cost savings can be passed onto consumers.
- 5.2 The Proposer believes that P426 will go some way to addressing the over-supply of security under the BSC by all parties, which has been looked at in previous Credit Cover Modifications, including [P326 'Introduction of a non-Working Day adjustment to the Credit Cover Percentage calculation'](#). P326 was raised by Haven Power Limited to introduce a method to account for reductions in Supplier demand on non-Working Days in the Credit Cover calculation and was implemented on 23 February 2017 as part of the February 2017 BSC Release.
- 5.3 A Workgroup Member asked if the proposed solution would be legally enforceable and felt this was the most important question for the Workgroup to consider. The Proposer was asked if the solution would apply to cash, Letters of Credits and insurance products used to provide collateral. The Proposer confirmed that he did not wish to discriminate and the Workgroup Member asked that a legal view therefore needs to be provided on all of these instruments.
- 5.4 The Proposer had indicated that, in the worked example, credit for BSC Parties A and B could be provided by another Party, C, who may not (currently) be a BSC Party. A Workgroup Member raised concern that in this scenario Party C would have to have control over the other two Parties, which would be a PCG arrangement (if Party C was indeed the parent company of BSC Parties A and B). The Workgroup discussed that Party C may have to become a BSC Party.
- 5.5 The Proposer explained his view that there is more credit being lodged than required, however, a Workgroup Member countered that this would always be the case as some companies choose to lodge more credit than required rather than constantly managing their credit levels. Also some BSC Parties may be foreign domiciled and therefore it's difficult to manage amendments to credit during the UK business day.
- 5.6 A Workgroup Member asked the Proposer why they could not use Metered Volume Reallocation Notifications (MVRNs) to consolidate their volumes into one Energy Account and then provide collateral on the combined position. The Proposer stated that they wanted a simple solution. A Workgroup Member explained that at New Electricity Trading Arrangements (NETA) go-live, MVRNs were designed rather than needing to manage volume from multiple BSC Parties in the same group. There were mixed views between the Proposer and some Workgroup Members on the merits of the proposed solution versus the use of MVRNs.

## 6 Wider market context and potential BSC impacts

- 6.1 Elexon presented an overview of wider market issues and potential impacts to BSC systems and processes to elicit Workgroup discussion.
- 6.2 The Workgroup continued to discuss the potential use of MVRNs as it was felt that this process assigned liabilities and exposure correctly but that the proposed solution may transfer the risk to the Balancing and Settlement Code Company (BSCCo).
- 6.3 The Workgroup discussed the periodicity of change of relationship and whether it should be annually, or on market entry/exit. The Workgroup felt it could be managed within the Elexon Portal and that the relationship should be validated. This may have to be signed off by a Company Director rather than an Authorised Signatory given the legal implications.
- 6.4 The Workgroup considered when the data should be combined and the Proposer agreed that the spirit of the Modification was to combine at the final stage of Credit Cover calculations.
- 6.5 The Workgroup considered transparency and how the market would be aware of a Party going into Credit Default, would it be on the combined or individual positions? If it was a Parent Company then it was felt that they would need to be published, and also should become a BSC Party.
- 6.6 A Workgroup Member stated that all scenarios need to be covered to protect the BSC. The solution should also be considered for cash collateral only as it's more liquid but obviously would be more costly to be provided than a Letter of Credit.

## 7 Progression Plan & Next steps

- 7.1 Elexon explained that an extension to the P426 Assessment Procedure will be requested at the next BSC Panel meeting on 14 July 2022 and, subject to approval, the revised Progression Plan will be shared with the Workgroup.

7.2 The second Workgroup meeting will be scheduled and will focus on further consideration of the legal implications and issues and the solution development.

## **8 Actions**

- 1** Elexon to provide an overview of the Credit Default and Payment Default processes at the next Workgroup meeting
- 2** Elexon to engage with its legal team to consider questions raised and to feed back at the next Workgroup meeting
- 3** Elexon to further develop the P426 solution based on feedback and discussion by the Workgroup, for consideration at the next Workgroup meeting