

P426 Workgroup 2 Summary

Summary

1 Welcome and Meeting Objectives

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

- Consideration of legal feedback on proposed solution
- Further development and refinement of proposed solution

2 Summary of WG1 and Actions

2.1 Elexon provided a summary of Workgroup meeting 1 which was held on 28 June 2022.

2.2 At that meeting the Proposer explained the issue and proposed solution and their views against the Applicable BSC Objectives. Elexon introduced the standard and specific Terms of Reference to be considered by the Workgroup and then provided an overview of the BSC Credit Cover arrangements. There was discussion on the points to be considered to help Elexon support the Proposer and the Workgroup in developing the proposed solution.

2.3 The three Actions captured from Workgroup meeting 1 had all been completed and would be covered under subsequent Agenda items at this Workgroup meeting 2.

3 Overview of Payment and Credit Default process

3.1 Elexon provided an overview of the BSC Payment and Credit Default process.

3.2 Elexon explained the timescales and consequences of entering Credit Default depending on the level, and also Payment Default and the Payment Default Timings. Elexon also explained the triggers of Default set out in [BSC Section H 'General'](#).

4 Development of proposed solution

4.1 Elexon reminded the Workgroup that the Proposal is to provide the option that BSC Parties are able to rely on shared credit arrangements and provision. The Energy Indebtedness of each Party shall be combined and that the Credit Cover Calculation shall then be performed on the combined position.

4.2 Elexon reminded the Workgroup that at the first Workgroup meeting they had agreed that the solution should apply to any unrelated Parties and not just those in the same group (i.e. with the same parent company).

4.3 The development of the proposed solution section of the Workgroup meeting was covered in three sections; Defining the entities, Provision of Credit Cover and Governance and process. This further developed the solution as introduced and discussed at Workgroup meeting 1.

5 Defining the entities

5.1 Elexon explained that practically the solution should only apply to BSC Parties as BSCCo has authority over BSC Parties. Given that BSC Parties can potentially join and exit the BSC at any time (subject to Market Entry and Exit processes) it was felt that the option to share Credit should be available at any time but that there needs to be consideration of the resource impacts of facilitating this.

5.2 Elexon explained the legal risks of the proposed solution and that irrecoverable Letters of Credit and Insurance and Cash, as provided for presently, are the safest methods of security. Security offered by a non-group company is least safe and affords more opportunity for attack from shareholders, insolvency practitioners and even by the company itself arguing against any security it has given.

5.3 Elexon explained that there was a need to ensure that this arrangement was not masking bad debt and therefore liability can't be shared if either Party has defaulted in the last 28 days. A Workgroup Member queried whether this could be gamed. Elexon explained that they would always know the individual Energy Indebtedness of each Party prior to combining for the purposes of the Credit Cover Calculation. The Workgroup Member stated that the

purpose of the current arrangements is to reduce the Default Funding Share. The Workgroup Member reiterated that in their view that the use of Metered Volume Reallocation Notifications (MVRNs) would provide the Proposer with the same outcome as the proposed solution without introducing additional risk on the BSC community and that this should be made clear in the Assessment Procedure Consultation.

- 5.4 The Proposer was asked their view on whether they would want the solution to apply to Parties in the same corporate group or to any two or more unrelated Parties. Their view at this point of the discussion was to keep an open mind and hear the Workgroup's discussion.

6 Provision of Credit Cover

- 6.1 Elxon explained that the combining of the Credit Cover calculation can either be done at the beginning or end of the process but that its recommendation was to combine at the end of the process, as this would mean less impact in terms of document and system changes and mean that Energy Indebtedness for individual BSC Parties would still be visible in the background. Elxon presented the algebraic Credit Cover calculations in more detail.
- 6.2 Elxon proposed that if one Party in the partnership (two or more Parties) were to enter liquidation, then the partnership in terms of combining Credit Cover will end and the enduring Party would need to provide collateral to cover their position within 1WD, ideally cash, which can subsequently be replaced with a Letter of Credit. A Workgroup Member queried the 1WD grace period as it could expose the BSC community to significant Credit liability. They suggested this should be a consultation question and that a risk matrix be produced to model low/medium/high scenarios. The Workgroup were invited to consider risk mitigations for discussion at the next Workgroup meeting.
- 6.3 In further discussing the issues, Elxon explained that it would be the responsibility of Parties combining their Credit Cover to ensure that their bank or insurance providers arranging their Credit are able to provide for all combined Parties, otherwise single Party rules would apply.
- 6.4 Elxon explained that the provisions in [BSC Section M 'Credit Cover and Credit Default'](#) 2.2 would apply as they do now, BSCCo would call on Credit Cover collateral as though they were dealing with a single Party. A Workgroup Member asked if there would need to be additional wording in the BSC to cover this. Elxon will consider this as part of the impact assessment as the solution is further defined.

7 Governance and process

- 7.1 Elxon explained that each Party entering into an arrangement would need to consent and sharing will not be effective until all Parties have separately notified the change. There will need to be Key Performance Indicators (KPIs) and/or Service Level Agreements (SLAs) for BSCCo to process the application and carry out appropriate checks.
- 7.2 Elxon raised a point about issues around potential sharing of insider information. A Workgroup Member clarified that the offence is to act upon inside information to manipulate the market, not necessarily to know it.
- 7.3 A Workgroup Member raised a concern that if non-cash collateral were provided there may be a risk that the underwriter (the bank or insurance provider) refuses to pay if the collateral is called upon by BSCCo. Elxon noted that there was a Modification ([P417 'Move the Letter of Credit templates and Approved Insurance Product requirements to the BSC Website for more efficient maintenance and simplification'](#)) which allowed the Letter of Credit template to be amended without the need to raise a new Modification, so P426 could make a change to the template if required.
- 7.4 A Workgroup Member made the point that the underwriter of the collateral (bank or insurance provider) may charge a premium for arranging Credit under a combined relationship and this cost may outweigh the benefit of the proposed Modification. Elxon's legal representative explained that even if the wording on the letter was right on our side, it doesn't stop the bank or insurance company trying to reject the claim. This will need to be drawn out in the consultation.
- 7.5 As the discussion was covering Credit arrangements, Elxon took the opportunity to promote a new BSC Issue which is due to be raised soon to review BSC Credit Cover arrangements, for which P426 Workgroup Members and others may be interested in joining.

8 Progression Plan & Next steps

- 8.1 Elxon explained that the BSC Panel had approved an extension to the P426 Assessment Procedure at its meeting on 14 July 2022. The P426 Assessment Report is now due to be presented at the February 2023 Panel

meeting, or earlier if possible. This will be post Assessment Procedure Consultation being issued to industry and a Workgroup meeting will be required to consider consultation responses.

- 8.2 Elexon explained that, as it was felt that another Workgroup meeting was required to consider the solution before a subsequent meeting to capture initial views on the Modification Proposal prior to consultation, the next Workgroup meeting would be arranged as soon as is practicable.

9 Actions

- 1** Workgroup Members to consider risk mitigation for the proposed solution in advance of or at the next Workgroup meeting, to support the Proposer
- 2** Elexon and the Proposer to consider the 1WD grace period for a single BSC Party to provide Credit collateral to cover their exposure in the event of their combined Credit Cover relationship with another Party being terminated due to the other Party's liquidation
- 3** Elexon to consider the wording of a clause in the Letter of Credit template to reference bilateral arrangements
- 4** Elexon to consider the risk that Parties enter liquidation at the same time, in addition to the scenario discussed where only one of the Parties enter liquidation
- 5** The Proposer to provide clarity on whether the solution should apply to Parties who are part of the same group only, or also to those who do not have an existing relationship, to then allow Elexon and the Workgroup to further develop the solution
- 6** Elexon to further develop the P426 solution based on feedback and discussion by the Workgroup, for consideration at the next Workgroup meeting