IGT132VV RFI Responses and Observations

On 25th October 2021 a Request for Information (RFI) was issued with regards to IGT 132VV. Three Shippers and Three IGTs responded to the RFI.

Questions included in the RFI were developed by the Workgroup in October 2021. As part of the development of the RFI, the Workgroup considered the four broad questions raised by Ofgem in their send back letter:

- What is the risk of not doing this?
- What does credit cover currently cost the market?
- Will the proposal hurt competition?
- What are the costs of intervention?

As part of the RFI the above questions were broken down even further, with two final sets of questions issued to industry (one for Shippers and one for IGTs)

Below sets out the questions issued as part of the RFI (grouped under the relevant Ofgem question), information received from respondents and observations drawn by the Workgroup at its December 2021 meeting.

IGT RESPONSES

Ofgem Question: What is the risk of not doing this?
1. How long do outstanding transportation invoice payments build up before action is taken by your organisation? **a) As soon as the payment is late** **b) Less than 3 months** **c) Greater than 3 months** **d) Other (please specify)** All three respondents stated "as soon as the payment is late"
2. Please explain what debt procedures your organisation would apply for unpaid invoices? Three responses were provided as follows: • One day past the due date an update is requested by email or telephone; Three days past the due date a follow up by email or telephone; Continued follow ups daily until payment received; The processes tend to be sufficient, except for when a Shipper's business fails and is therefore unable to pay. • Contact the Shipper with a notice of "speaking to legal" regarding the debt after 2 months; and • A notification is sent to the Shipper advising that Late Payment interest is now being applied to that invoice total and a request is sent again for payment to be made. If payment is not received after that sanction options would be explored. <u>Workgroup Observation</u>: The responses show that there is not a consistent system that is being used by IGTs for debt procedures with regards to unpaid invoices. In addition to this there are limited actions that IGTs can take.

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3. What sanctions are available to your business and when would it apply them in the case of debt? Three responses were provided as follows: • IGT UNC Section G clause 14 allows us to apply sanctions preventing a Shipper from registering additional MPRNs into their portfolio where outstanding debt exceeds £10,000. However it provides no protection against further debt accruing on their existing portfolio; • Late payment fees are invoked. If the debt is over £10,000 we can stop companies from connecting to our networks through Xoserve; and • Options are available to limit and contain potential debt. From calling in a solicitor and other third parties to collect the debt, to preventing registrations of the Shipper party via the Gas CDSP. Workgroup Observation: The responses show that there is not a consistent system in place and although various action could take place to limit further debt it does not help relinquish the current debt has been built up.
4. What are the impacts of debts not being paid on your business? Three responses were provided as follows: • Any unpaid debts will have an immediate impact on cash and cash forecasts. Depending on materiality of the amounts involved it may impact funds available for future investment in gas networks; • The impact of debts not being paid to our business would be cash flow problems and Suppliers loss; and • In the short term there is limited direct impact from debts building up. However, in the longer term such events (where bad debt in particular builds up) are then accounted for in annual budget planning which ultimately requires the balance sheets to allow the licenced entity to continue to function at the potential expense of some of its activities. These are to be assessed as and when required. Workgroup Observation: The responses show that cash flow will be affected for all the respondents when debts are not paid, ramifications from this could be that IGTs may not be able to finance other licensed activities which could impact the consumer, but this varies with each IGT as they each handle cashflow in different ways.
8. What are the impacts of Shipper failures on your organisation? Three responses were provided as follows: • It could result in up to 2 months of non recoverable transportation revenues. This has an immediate impact on cash, and cash flow forecasts; • Increase in bad debt within the organisation and results in a loss of cash flow; and • Affects the organisations cash flow and thus ability to fund its licenced activities from a loss of revenue without a means of recovering bad debt. Large and multiple such Shipper failures therefore represent a risk that resources are required to be taken away from the end consumer in operational tasks like interruptions and maintenance with these required to maintain the business as a whole. One response was confidential and is to be provided to Ofgem.

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<u>Workgroup Observation</u>: The responses draw a similar picture to the responses that were received for the question regarding bad debt – depending on how cash flow is managed with IGT it may affect other licensed duties which in turn could affect the consumer.

Ofgem Question: What does credit cover currently cost the market?

5. In the year 2020/21 how much do you charge each Shipper short code for transportation per month? What is the average, the minimum and the maximum per Shipper per month? (Potentially commercially sensitive)

Confidential responses provided, these will be passed onto Ofgem.

<u>Workgroup Observation</u>: The responses to this question demonstrate the financial risk to the IGTs in comparison to the Shippers costs for credit cover (see responses to Shipper question 1). The two responses should be aligned to show what the cost are for the market.

6. Is your organisation likely to implement the credit cover offered by Modification 132VV (Introduction of IGT Code Credit Rules) if it is implemented? If so, how and in what capacity will it be implemented?

Three responses were provided as follows:

• We would ask all Shippers active on our network to provide some form of credit cover, in accordance with the provision of Modification IGT132VV; and

• We would implement this and we would write a process of how this would be implemented within finance. One response was confidential and is to be provided to Ofgem.

<u>Workgroup Observation</u>: The responses show that the respondents would implement the credit cover offered by Modification IGT132VV if it was to be implemented.

7. Which of these options would your organisation accept as credit cover? Multiple options may be applicable

- Parent company guarantee
- Letter of credit
- Cash
- Escrow account deposit
- Other (please specify)

All respondents stated "letter of credit", two respondents stated "escrow account deposit" and two respondents stated "cash" and "parent company guarantee". A respondent also stated that they would be open to a number of collateral options to accommodate the Shipper parties, but a "Letter of Credit" would be the preferred.

<u>Workgroup Observation</u>: The response to this question should be looked at in line with the Shipper responses to question 10, to work out the cost to Shippers. Shippers have stated that parent company guarantees, letter of credit and cash would all be accessible to them, therefore it could be drawn that there is shared ground between the IGTs and Shippers with regards to credit rating options.

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10. What factors in the credit process described in Modification IGT132VV (Introduction of IGT Code Credit Rules) will impact efficiency and why? Please provide the rationale. **- Positively** **- Negatively** **- Neutral** Two respondents stated it affected them positively: • Having credit protections in place will provide greater certainty over cash inflows, and in turn greater certainty over funds available for investment in gas networks. The protections will allow for a reduced focus on time spent credit checking, chasing debt, and generally spent discussing the financial position of Shippers and potential implications of Shipper failures; • It is acknowledged that Code Credit Rules aren't a silver bullet, and work to solely help limit the bad debt IGTs incur rather than remove it in its entirety. This does however present an improvement in the efficiency of how IGTs can manage the financial security of their networks with arrangements adopted and utilised in line with their counterparts in the Gas and Electricity markets; and • In terms of the IGT UNC itself, efficiency is presented by this change due to stripping out individual network code credit rules to establish a standardised approach for all IGT and Shipper parties. Removing the option of differing approaches to be adopted and thus potentially causing confusion and increased costs for the market to contend with. One respondent stated it had a neutral affect. Workgroup Observation: The responses show that the credit process described in the Modification IGT132VV is mainly viewed positively, particularly as it would offer more clarity and certainty.
9. How many Shipper licenced entities (short codes) do you have agreements with? How many registered companies do they represent? How many company groups do they represent? Confidential responses were provided, these will be shared with Ofgem.
12. Does your organisation believe there are any key areas of concern in this Modification IGT132VV (Introduction of IGT Code Credit Rules) that have not been identified? Does your organisation have any other elements that you would like the Modification to include? Two responses were provided as follows: • What happens if the Shipper refuses to pay? How is this enforceable?; and • It is felt the Workgroup have done well to assess the content of the Code Credit Rules and their impact on the market. While it is acknowledged this Modification hasn't been accepted with welcome arms it has been widely acknowledged that its intent is supported with only the application and details of such arrangements requiring amending, which have been made through the Workgroup's efforts.
Ofgem Question: Will the proposal hurt competition?
11. How might Modification IGT132VV (Introduction of IGT Code Credit Rules) impact competition for IGT's and if so, how? (Please provide supporting evidence where possible)

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Three responses were provided as follows: • By removing some of the financial risks to IGTs may encourage more parties to enter the market; and • It is not anticipated IGT132VV will have an impact on competition between IGTs. Because of the nature of the methodology within the code credit rules the requirement and cost to implement is theoretically scalable to the business. i.e., the cost for IGTs to maintain is based on administrative activities of the arrangements rather than the collateral itself which lies with the Shippers. This therefore allows for IGTs to assess and monitor the risk of debt to their business and implement code credit arrangements as and when that risk rises. Workgroup Observation: The responses show that the potential credit rules generally will have a positive impact on competition by offering less financial risk and the ability assess and monitor the risk of debt more accurately, this in turn should make competition better for the IGTs.

SHIPPER RESPONSES

Ofgem Question: What are the costs of intervention?
1(a) What is the admin cost for introducing credit rules for new entities (e.g. new IGTs) for your organisation? **a) less than £10k** **b) between £10k and £100k** **c) over £100k?** The responses ranged between less than £10k and £10k and £100k. The costs would be for new arrangements as these are new legal entities, Parent Company Guarantees or Letters of Credit (difficult to estimate cost as it depends on how much negotiating is needed) and new processes to monitor (the different collateral in place, the different rules, and the different renewal dates). One respondent stated that once credit cover is set up and it does not change regularly, these costs would be on an ad hoc basis. Workgroup Observation: The Workgroup agreed that this response should be aligned with the confidential response to question 5 for IGTs, in order to show the cost to risk comparison.
1(b) Are there any other factors influencing admin costs for introducing credit rules? Two respondents agreed that this may vary depending on who takes this up and what type of collateral is required. Initial set up of reports in SAP will be dependent on who chooses to introduce credit cover as this change is not making it mandatory for an IGT to introduce credit cover. Other costs identified were staff resources to implement new procedures. Workgroup Observation: The answer provided to Ofgem will give further confidential information about the size of the Shipper in order to give perspective to the responses.
2. What is the percentage rate for which you would obtain credit for IGTs?

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One respondent was not comfortable to disclose this information, one respondent did not have an answer to this question at the time and a third respondent provided a confidential response which will be provided to Ofgem. Workgroup Observation: The responses to this question should be read in line with the IGT response to question 5.
3. For comparison: What is the cost of maintaining credit cover rules for the Gas Distribution Networks (GDNs) under the UNC? a) less than £10k b) between £10k and £100k c) over £100k The responses ranged between £10k and £100k and over £100k. These costs were made up of: • Monitoring credit exposure daily; • Updating credit where necessary and the cost of getting it signed off as there are approximately 6 people involved in every request; and • Letter of Credit coverage. One respondent stated there would be annual running costs for maintaining credit cover. Workgroup Observation: The Workgroup agreed that this response should be aligned with the confidential response to question 5 for IGTs, in order to show the cost to risk comparison.
5. What are the anticipated impacts of additional credit cover and what would be the level of impact to your business? **a) high** **b) medium** **c) low** Two respondents answered low and one answered medium. The respondents stated that it will depend on how many IGT's take this up, whether they will accept PCGs and how much credit is required. Other impacts recognised were additional resources required to monitor and maintain adequate LC facility. Cash requirements would be covered through existing financing set-ups. Workgroup Observation: The Workgroup agreed that the responses were predictions and that it is difficult to anticipate impacts of a credit cover procedure that is not yet in place. It was also acknowledged that the existing finance set up would be able to take on the cash requirements and that why two respondents answered that the impact would be low.
6. Are there any reasons why additional costs for IGT transportation credit cover would not be passed onto consumers? Please specify. One respondent could not see any reason why additional costs could not be passed onto the consumers. Two respondents stated that consumers on a fixed contract could not have costs passed on as they are on fixed prices agreements. It may be that costs could not be passed on to the consumer until they have moved onto a new tariff. Workgroup Observation: It was observed by the Workgroup that the additional costs would be passed onto to the consumers and the only exemption highlighted by the respondents were that some consumers were contracted to a fix tariff, but these contracts will eventually need to be renewed. Therefore, Shippers should be able to get the money back for the credit cover costs.

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11. What factors in the credit process described in Modification IGT132VV (Introduction of IGT Code Credit Rules) will impact efficiency and why? Please provide the rationale. **- Positively** **- Negatively** **- Neutral** One respondent stated the Modification would have a neutral effect on the efficiency of their organisation. Two stated that it would have a negative impact on their organisations and the reasons for this are: • That there would be no uniformity in the method each IGT uses, so more time will be spent figuring out the rules for each IGT and keeping track of what credit needs renewing and how it can be renewed; • That this will all need to be documented and monitored on almost a permanent basis, there also could be a situation where multiple renewals happen at the same time; and • This would be an added layer of administration for SoLR and given the current energy market crisis this is happening on a much more frequent basis. Workgroup Observation: The concerns observed were that there may not be uniformity in the method that each IGT uses, however there is currently no uniformity in place as things stand and the purpose of Modification is to introduce a form of credit cover uniformity applicable to all Shippers and IGTs.
13. Does your organisation believe there are any key areas of concern in this Modification IGT132VV (Introduction of IGT Code Credit Rules) that have not been identified? Does your organisation have any other elements that you would like the Modification to include? One respondent provided no further information. One respondent stated that they understood the requirement for cover, but ideally it would be centrally managed. One respondent stated that it needs to be made clear within the Modification that this is for transportation charges only and not include any other charges such as ERC, Rental, Job and Must Read. Workgroup Observation: Credit cover is for transportation charges only and this could be made more clear.
Ofgem Question: What does credit cover currently cost the market?
4. For comparison: What is the percentage rate for which you would obtain credit for the Gas Distribution Networks (GDNs)? (Potentially commercially sensitive) Two did not respond to this question. One respondent provided a confidential response to be provided to Ofgem.
7. What size is your Shipper organisation(s) (in total)? **a) Small - Less than 100k supply points** **b) Medium - 100k to less than a million supply points** **c) Large - a million supply points or above**

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Two respondents state that they are a large (a million supply points or above) Shipper organisation, and one was a medium (100k to less than a million supply points) Shipper organisation. Workgroup Observation: The response for this question should be looked at in line with the responses to questions 5 and 9 of the IGT responses.
8. How many IGT licenced entities do you have agreements with? How many registered companies do they represent? How many company groups do they represent? One respondent has agreements with 14 IGT's, one respondent has customer-vendor relationships with 8 IGT groups and the third respondent has 11 -13. Workgroup Observation: The responses to this question given an idea of the amount of work that would be required, as not all Shippers have agreements with IGTs.
10. Which of these would be options available to you? Multiple options may be applicable Credit rating **- Parent company guarantee** **- Letter of credit** **- Cash** **- Escrow account deposit** **- Other (please specify)** All three respondents stated these options would be available to them; parent company guarantees, letter of credit and cash. One respondent stated all the options would be available to them and in addition escrow account deposits too. Workgroup Observation: The response for this should be looked at with the IGT response to question 7. Looking at both responses it shows that there is an agreement of the credit rating methods, therefore it could be drawn that there is shared ground between the IGTs and Shippers with regards to credit rating options.
Ofgem Question: Will the proposals hurt the competition?
9. Will the IGT UNC credit cover Modification (IGT132VV) significantly impact your organisation's overall credit position? Please explain how and whether that would be positive or negative. Two respondents considered it unlikely to have a negative material impact to the overall company position or a negligible impact. One respondent stated that there would be a significant impact on their organisation, but it would be difficult to quantify until the amount of credit required is known. The respondent stated that the likelihood is that it will run into millions of pounds of extra credit which would be thousands if not tens of thousands of pounds of extra costs in fees alone as well as needing a member of staff who's role could purely be managing this credit cover, especially in the current times where things are extremely unpredictable.

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Workgroup Observation: It was observed by the Workgroup that the overall credit position of a Shipper being affected by the Modification would be difficult to predict and the size of the organisation needs to be taken into account. It was assumed that the changes brought in by the Modification would impact the overall credit positions of the smaller Shippers more negatively, however larger organisation have aired concerns with the Modification and see it as potentially having a negative impact on their overall credit position.
12. How might Modification IGT132VV (Introduction of IGT Code Credit Rules) impact competition for Shippers and if so, how? (Please provide supporting evidence where possible) One respondent stated that they do not provide or ship to any other Supplier. The respondent stated if this is an issue for a large Shipper, it's likely to be an even bigger issue for medium and small Shippers as they will have less availability of credit, less cash and may not be able to afford the extra manpower. Another respondent stated the work involved in managing this is almost the same regardless of the size of the Shipper, so the smaller the Shipper the more the impact. Workgroup Observation: The responses state that it is an extra measure, and that smaller Shippers may have the same costs for credit cover as the larger Shippers and this may therefore effect competition negatively.

QUESTION CATAGORISATION

What Are The Costs Of Intervention?	What Does Credit Cover Currently Cost The Market?
What costs could be passed through to consumers?	What credit cover costs do shippers currently face?
How many more IGT's would be likely to implement credit cover arrangements under new rules?	Do credit cover costs get passed through to consumer bills via shipper fees?
Will the level of credit cover required by IGT's currently increase or decrease?	What credit cover costs do consumers currently face?
What credit cover level will the new rules require IGT's to request from shippers?	How many IGT's currently require credit cover?

Will The Proposals Hurt Competition?	What Is The Risk Of Not Doing This?
Will shippers face different levels of additional costs?	What costs do consumers face when IGT's face bad debt costs?
Do Smaller shippers face higher costs under new proposals?	Are consumers impacted when a supplier fails?
	What is the risk that further situations arise where IGT's are exposed to bad debt costs?
	What is the risk that bad debt exposure leads to IGT failure?
	What impact would an IGT failure have on consumers?
	What impact would an IGT failure have on the market?