

Reference

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Date

4 September 2020

Mick Watson
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OFGEM
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Dear Mick,

Managing network charge bad debt

Thank you for the opportunity to respond to Ofgem's consultation on its proposals to manage network charge bad debt. Our response is not confidential and may be published by Ofgem.

We welcome Ofgem's proposals for both addressing any bad debts arising from the COVID-19 Network Charge Deferral Scheme (NCD) and beyond that on an enduring basis within the RII02 price control. This is consistent with the approach agreed with Ofgem when the NCD was implemented and going forward aligns the transportation revenue risk profile with Ofgem's broader RII02 cost of capital proposals. We therefore support Ofgem's preferred Option 3 of introducing a Bad Debt term as a pass-through item in the gas transporter licence and as part of this including a provisional allowance which is trued up through the annual iteration process.

We understand detail concerning how provisional allowances will be assessed and how the proposal will be applied are still being developed and look forward to further discussion with Ofgem to clarify how it will operate in practice.

In discussions with Ofgem we have suggested that given the risks associated with implementation of RII02 by 1 April 2021 that we would support de-linking this proposal from the overall RII02 licence consultation process to ensure it can be applied to any bad debt associated with the NCD scheme. We recognise this may be difficult for Ofgem and therefore suggest that should RII02 be delayed, that in respect of the NCD scheme, we utilise the existing RII01 Miscellaneous Pass through term to recover any costs arising.

Our answers to Ofgem's specific questions are detailed below:

Q1: Do you agree that our proposals would allow the recovery of bad debts, by network licensees, relating to Network Charge Deferral scheme (COVID19) in 2021-22?

We agree that Ofgem's proposals and preferred Option 3 of introducing a Bad Debt term as a pass-through item in respect of the NCD scheme would allow recovery of bad debt by network licensees subject to clarity on the detail mechanisms and rules that will be applied to the licence and associated RIGs. Further to this, we request that Ofgem considers extending this provision to recovery of bad debt arising from any shipper in this final year of RII01 whether they have participated in the NCD scheme or not.



As Ofgem has recognised, there is a risk around RIIO2 delivery for 1 April 2021 and therefore we suggest that as part of this proposal Ofgem gives due consideration to alternative risk mitigation measures that could be applied if needed. The two options that we believe could be implemented are either to de-link the Bad Debt pass through condition from the main RIIO2 licence consultation process to allow it to be implemented by 1 April 2021 on its own, or in the case of gas distribution networks, utilise the Miscellaneous Pass through term that already exists in the licence.

Recognising that the former may be difficult from a process management perspective, we suggest that Ofgem considers utilising the latter should bad debt arise from the NCD scheme and the RIIO2 implementation risk materialise.

Q2: Do you agree with the introduction of a pass-through term in the RIIO2 licence as an enduring solution for the recovery of bad debt?

We agree with the introduction of a pass-through term as an enduring solution for the recovery of bad debt, as it better aligns gas transportation revenue credit risk with Ofgem's implied low risk/low return RIIO2 cost capital proposals. Gas transporters mitigate their revenue risk through UNC credit and security arrangements, but are nevertheless exposed to defaulting shippers. While this has been a rare occurrence to date, the increasing levels of competition and financial strains in the gas market even before COVID-19 are becoming more apparent, increasing the risk gas transporters with limited means to manage such exposure.

Finally, in relation to both Q1 and Q2 and noting Ofgem's indicative timetable, there may be a need to clarify the timing of provisional bad debt allowances to enable GDNs to calculate and issue final transportation price notices at the end of January in each formula year.

I trust this response is helpful and look forward to further dialogue on development of the mechanisms and processes to implement Ofgem's proposals in the licence and the RIGs.

Yours sincerely,

Paul Rogers

By email