
Wholesale Retail Code Change Proposal – Ref CPW095

Modification proposal	Wholesale Retail Code Change Proposal – CPW095: Maintaining the Credit Support Requirement
Decision	The Authority has decided to approve this Urgent Change Proposal, subject to modifications
Publication date	15 April 2020
Implementation date	08:00 on 16 April 2020

Background

As a result of the Covid-19 pandemic, the business retail market faces a number of pressing issues. In March 2020, the UK government issued guidance and imposed legislative measures to help reduce the spread of Covid-19, by requiring that, unless exceptions apply, businesses and premises should be closed and large gatherings, non-essential travel and any other such activities should be avoided. Many businesses and workers are in self-isolation and have implemented social distancing.

It was anticipated that this would likely to lead to significant reductions in the levels of water and wastewater services used at a number of business premises. Therefore, to provide immediate interim relief to customers and Retailers, the Authority raised two Change Proposals which were subsequently approved and implemented on 30 March 2020:

- [CPW091](#) - to allow Retailers to temporarily apply the vacant flag in the Central Market Operating System (CMOS) where premises have closed down due to Covid-19; and
- [CPW093](#) - Which enables Retailers to temporarily defer up to 50% of Wholesale Charges in March 2020, and from Settlement in April and May 2020.

The modification proposal

This Urgent Change Proposal was raised by Thames Water (the Proposer) to mitigate the risk of increased Wholesaler bad debt where a Retailer that post-pays defers payment in accordance with CPW093. The Final Report highlights that the

impact of CPW091 would first be felt in the May P1 Settlement Period (in the P1 Settlement Run that will be completed in April 2020). It also sets out a worked example of how Wholesaler exposure might be increased where payment is deferred by a Retailer that post-pays.

To address the identified issue, the Proposer has recommended that the Credit Support Requirement (CSR) is maintained at the March 2020 level where Retailers that post-pay elect to defer charges using CPW093. The March 2020 CSR level will be used instead of the amount that would be adjusted as it usually would to reflect lower settlement charges that will result from implementation of CPW091. Alternatively, a Retailer is able to pay the wholesale charges in full and benefit from lower CSR which result from lower P1 wholesale charges due to increases in vacant premises and lower levels of consumption.

The Panel's Final Recommendation Report highlights that there have been discussions with Water UK and engagement with the Authority but there has not been an industry consultation due to the urgency of the proposal. It is also stated that Retailers may object to the retrospective nature of this Urgent Change Proposal where Credit Support Notices have already been issued and/or Retailer CSRs have fallen below the original March 2020 level. For example where a Retailer has already reduced its credit support by modifying Guarantees, Letters or Credit or Surety Bonds.

Panel recommendation

Seven out of 11 Panel Members confirmed that the change is an Urgent Change Proposal at its meeting on 15 April 2020. At the same meeting, the Panel considered the Urgent Change Proposal.

The Panel recommended that the Authority approve the Urgent Change Proposal. Six out of the ten Panel Members¹ in attendance at meeting abstained from voting. Four Panel Members voted in support of the Urgent Change Proposal. This recommendation has been made on the basis of improving the principles of proportionality, simplicity, cost-effectiveness and security and the Business Terms Objectives. The recommended implementation of the Change Proposal is 16 April 2020 as this is the last point at which CSR are issued.

The Panel Members that supported the Urgent Change Proposal agreed with the rationale put forward by the Proposer. They considered that the proposal protects both customers and Wholesalers at a time where Wholesalers were exposed to additional risk of Retailer default. It was noted that the amount of CSR required from Retailers who elected to defer payments will not be increased above the CSR that

¹ One Panel Member who had supported the urgency was not available to vote on the change proposal.

was required to be lodged for the March 2020 P1 Settlement Run, which is being preserved as the status quo.

The Final Report states that the Panel Members who abstained from voting expressed concerns that there was a lack of information regarding the values that would be at risk in the event of a Retailer defaulting. Further, some Panel Members felt unsure where the balance of risk should sit between Retailers and Wholesalers. Whilst acknowledging the urgency of the proposal, some expressed concern that there was a lack of information which they considered might lead to further unintended consequences. Some of those that abstained 'acknowledged the principle behind the change'. One suggested that the change might reduce the risk of adverse customer impacts in the long term. However, it was suggested that it might exacerbate the risk of Retailer failure in the short term, which would equally have an immediate adverse impact for customers.

Our decision

We have considered the issues raised by the Change Proposal and the supporting documentation provided in the Panel's Final Report and have decided to approve the Urgent Change Proposal, with some amendments to the legal drafting. The amendments that have been made to the legal drafting can be found in Appendix 1 of this document and have been made to add clarity and ensure that the proposal has the desired impact – where Retailers elect to defer less than 50% of charges, they will still be required to lodge CSR at the March 2020 level.

Subject to the amendments to the legal drafting as detailed in Appendix 1, we are supportive of the Urgent Change Proposal which seeks to rebalance Wholesaler risk exposure following the implementation of CPW091 and CPW093. The intent of those Change Proposals was not to reduce the level of collateral that Retailers are required to lodge. We do not consider that it is in the interests of the market or customers to reduce the CSR given the temporary nature of CPW091 and CPW093 and because there will ultimately be a necessity to reverse any reduction in CSRs in any event.

We acknowledge concerns that were raised by Panel Members at the Urgent Panel Meeting regarding decision making at speed. The current circumstances in which the sector is operating in are extreme, and we consider that making swift and timely interventions is necessary in these circumstances and we would encourage Trading Parties and Panel Members to continue to have this as a consideration during this period of disruption. We acknowledge, however, that there is a risk of unintended consequences arising when urgent code modifications need to be made at speed. As such, it is important that Panel Members are appropriately challenging proposals and providing a definitive view on whether or not they support a proposal, rather than

abstaining. This assists the Authority with its decision making as it provides greater insight into the benefits and issues that may be applicable to any given proposal.

We have concluded that the implementation of CPW095 will better facilitate the principles of the Wholesale Retail Code as detailed in Schedule 1 Part 1 Objectives, Principles and Definitions and is consistent with our statutory duties.

We consider that the Urgent Change Proposal will further the principle of proportionality, simplicity, cost-effectiveness and security and the Business Terms Objectives. This is because the proposal is a temporary change, which is consequential to CPW091 and CPW093 and seeks to rebalance the risk of a Retailer default for Wholesalers. The Urgent Change Proposal also seeks to enable the market to continue to function effectively. Therefore, we have decided to approve this Urgent Change Proposal with an implementation date of 16 April 2020.

Decision notice

In accordance with paragraph 6.3.7 of the Market Arrangements Code, the Authority approves this Urgent Change Proposal.

Georgina Mills
Director, Business Retail Market

Appendix 1 – amendments to legal drafting

9.12.3 (c) For the purposes of the Credit Support Notices generated from the April 2020, May 2020 and June 2020 P1 Settlement Reports, where the value of the Credit Support Requirement is lower than for the March 2020 P1 Settlement Report, and, consequently, the Credit Support Amount is lower than for the March 2020 P1 Settlement Report, the Contracting Retailer must provide and maintain the Credit Support Amount at the March 2020 level, until such time as the issue of the Credit Support Notice generated from the July 2020 P1 Settlement Report, or such other time, as ~~notified by the Authority~~ **notifies the Market Operator**.

9.12.3 (d) The requirement in 9.12.3(c) shall only apply where the Contracting Retailer has an unpaid Suspension Percentage or Deferred Amount, or any portion of said Suspension Percentage or Deferred Amount is unpaid, when the relevant Contracting Wholesaler issues the Credit Support Notice prior to issue of the Credit Support Notice generated from the July 2020 P1 Settlement Report, or such other time, as the Authority notifies the Market Operator.