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Date: 21 April 2020

Finance & Governance
Ofwat
21 Bloomsbury Street
London
WC1B 3HF

By e-mail: covidbusinessretailmarket@ofwat.gov.uk

Dear Sir,

LIQUIDITY AND BAD DEBT CONSULTATION

In these unprecedented times, water companies face several challenges with the health, safety and wellbeing of our employees and customers paramount and our number one priority during the COVID-19 pandemic. Many of our employees are designated key workers and are delivering the best possible service to customers during this challenging time.

In respect of this consultation which focuses on the liquidity and bad debt challenges within the Non-household retail market (for both retailers and wholesalers) we accept that it is essential that a holistic approach is taken to address these issues. However, we need to ensure that short and long-term risks of any changes are appropriately distributed across the market and that the financeability of wholesalers is not compromised by supporting liquidity in the market nor the risk of retailer default.

We have included detailed responses to certain questions in Appendix 1.

If you have any queries, or would like any further detail, please do not hesitate to contact us at finreg@southwestwater.co.uk.

Yours sincerely

[redacted]

Louise Rowe
South West Water Finance Director

APPENDIX 1

1. **Do you agree with these objectives as set out, which will guide our decisions about what are the preferred options?**

   We support the overall objectives within the consultation which are focused on the impact of Covid-19 and are not relating to the existing position of the NHH retail market.

Questions 2 and 3 are for Retailers (optional for Wholesalers)

2. **Excluding customers with temporary vacancy flags, what percentage of remaining wholesale charges are you currently able to recover from customers each month? Please explain why these customers, who are still open for business, are late paying (or not paying in full). Please also provide evidence to support your response.**

3. **Please explain how you expect your response to question 2 to change over the next month or two.**

For all trading parties:

4. **Which option for dealing with the remaining liquidity gap facing business retailers do you think would be in the best interests of customers, the market and best reflects the objectives we are trying to achieve? Please explain your view and provide supporting evidence.**

   We believe that it is important that retailers continue to use all options available for liquidity, including targeting cash collections from customers; existing credit arrangements (or potentially new credit options such as parent company guarantees where this option is not already in place); accessing government support (including loans and staff support) with the deferral of payments to wholesalers considered as the last resort.

   We support a minimum level of payments that retailers are required to pay and agree that this should be significantly higher than the 50% initially allowed for March and April 2020, however 70% of monthly charges still reflects a considerable risk to wholesalers for non-payment. Assuming all retailers take full advantage of the 50% and the 30% deferrals to the end of July this equates to c.40% of revenue over 5 months (taking account of the expected demand falls already seen using the recent code changes) which will be above the 30% risk in the consultation – if payments for deferrals for March and April are not required.

5. **How should we determine the financing costs associated with any liquidity provided by wholesalers? Please explain your view and provide supporting evidence.**

6. **Do you agree that the financing costs associated with any liquidity provided by wholesalers should be borne by retailers? Please explain your view and provide supporting evidence.**

   We agree that as with any liquidity support the cost of providing this should be borne by the retailer, however this needs to be proportionate and reflect the costs incurred by the wholesaler as well as setting the right incentives for performance and focus on payment recovery.

7. **Do you agree that retailers should receive liquidity support at least to the end of July 2020? And that all additional liquidity provided by wholesalers should be repaid by the end of December 2020?**

   We absolutely agree that liquidity support should be time-limited and used to reflect the impacts directly as a result of COVID-19 and not to support existing retailer liquidity issues and would therefore support the position up to July 2020.

   In terms of the requirement for full payment of the deferred amounts we believe clarity is needed on how this is expected to be profiled over the period to December 2020 – not assuming a balloon payment can be made at the end of the December 2020.

   As a result, we believe the changes in the code should set a minimum amount of repayments due from August 2020 and that for non-payment a retailer would be assessed as in default if the current and deferred charges are not paid.

8. **Should retailers incur all bad debt costs from non-household customers defaulting or should some of these costs be recoverable beyond a pre-determined threshold? Please explain your response and provide supporting evidence.**

9. **If bad debt costs from non-household customers defaulting should be recoverable beyond a pre-determined threshold, then do you agree that retailers should expect to manage all bad debt costs up to 2% of their turnover, or the level of bad debt from their most recently audited level +1%, whichever is the greater?**

10. **Where bad debt costs from non-household customers defaulting exceed a predetermined threshold, should these costs be shared between retailers and non-household customers, and in what proportion, or should they be born wholly by customers? What relevant precedents are there (including in other sectors)? Please explain your response and provide supporting evidence.**

    We have not given a response to questions 8-10 as these largely relate to the expected impacts for retailers.

11. **Do you do you agree there is a case for protecting wholesalers from the bad debt exposure associated with the liquidity measures? To what extent do you think the wholesale price control mechanism provide sufficient protection to wholesalers for Covid-19 related bad debt? Do you think we should amend the totex sharing factors or introduce a cap – for example, a proportion of wholesaler business market turnover?**

    We agree that where liquidity is given by wholesalers in support of the whole NHH retail market they should be protected from the additional bad debt exposure they face – which could impact on financeability of the wholesaler (not just liquidity). The current market codes already give a certain level of risk to the wholesalers and this has been the basis for price controls set for PR19. The proposed liquidity support given to the market increases this risk significantly above the existing levels assumed, with the value of debt with retailers increasing as well as the potential higher risk of retailer failure in these unprecedented times. Therefore, we support the need to consider further mechanisms (or amendments to existing ones) to appropriately and proportionately share the impact of these changes.