

OFWAT – BUSINESS RETAIL MARKET NEXT STEPS CONSULTATION

13 July 2020

Introduction

Please find attached the Pennon Water Services response to the above Ofwat consultation.

Covid-19, while incredibly challenging to all stakeholders, has demonstrated several potential positives to shape the NHH retail market going forward. For the PWS management team key positives are:

- Swift and decisive consultation and change
- Effective stakeholder collaboration
- Focus on known market weaknesses that need to be improved quickly, primarily data and meter reading

Since March, PWS has worked hard to ensure it adapts positively to the new environment generated by Covid-19 and has closely monitored market changes. Our approach has been to support our customers while ensuring PWS is in a sustainable position and setting an example in the market.

This consultation is very comprehensive, and we have answered as fully as possible in the given time. The interim market changes were very welcome and effective and unwinding them is probably harder than their implementation. Ofwat need to consider whether introducing new measures are the best solution or consider whether ensuring the existing mechanisms are applied fairly and evenly across all Trading Parties is more suitable. The timing of any reversion of a change is also critical because Covid-19 and government rules may restrict Retailer's ability to implement them fully.

Once changed back, the establishment of a sustainable market is a priority and our view is the main wins lie in addressing the meter reading process and ownership and proportionally incentivising all market participants in designing and implementing a comprehensive data correction project.

Along with the work on water efficiency and bilaterals the natural outcome of these projects will be a transformed experience for all customers.



Richard Stanbrook
Managing Director

16 July 2020

Consultation Questions

Temporary Liquidity Support

- 1. Of the three options identified in relation to extending liquidity support, which option do you support and why? Please explain your answer and provide supporting evidence wherever appropriate. Which option is most compatible with furthering customers interests and why?**

PWS has not utilised this support and our plans do not include its use in the future. We therefore believe that the views of other Retailers who will be affected by this decision should take precedent over any view we may have.

This response does not in anyway minimise the serious affect that Covid 19 is having on all Retailers. Any measures that support Retailers and their ability to serve their customers are very welcome.

- 2. If we were to implement option 2, should we retain the existing capped amount of liquidity support (i.e. 40% of primary charges from March to July), or should this be reduced to a lower level (e.g. 30%, or 25%)? Please explain your answer and provide supporting evidence wherever appropriate.**

Please see above answer

- 3. If we were to implement option 2, should we continue to allow Retailers to opt into the scheme at any time up until October 2020? We also welcome stakeholder views on the most appropriate way a cap could be implemented into the current mechanism. Please explain your answer and provide supporting evidence wherever appropriate.**

To ensure fairness to all Retailers, the opt in option needs to be available to all Retailers because circumstances may change over time. The effect of Covid-19 on customers may not yet be fully visible and a slow down in payments to Retailers may not be currently showing. Slower collections and more bad debt may yet hit Retailers and some may find themselves in need of the scheme in the coming months rather than now.

It seems from the data available that Ofwat is best position to identify a suitable cap mechanism that creates a fair challenge

Unwinding Temporary Liquidity Support

- 4. Of the three options identified in relation to unwinding liquidity support, which option do you support and why? Please explain your answer and provide supporting evidence wherever appropriate. Which option is most compatible with furthering customers' interests and why?**

Option 3 appears to offer the best solution in that Wholesalers and Retailers can agree their own repayment profile whilst at the same time having a regulatory backstop which protects all parties. This builds trust and allows wholesaler/retailer negotiation

- 5. Under option 3 do you agree that 33% of deferred wholesale charges should be repaid by end November 2020 and that 66% should be repaid by end January 2021? Please explain your answer and provide supporting evidence wherever appropriate.**

Yes – this provides a broad regulatory structure and a framework for detailed agreement between Wholesalers and Retailers unilaterally.

Temporary Vacancy Flag

- 6. Do you agree that the option for Retailers to use the temporary vacancy flag should be allowed to expire on 31 July 2020? Please explain your answer and provide supporting evidence wherever appropriate.**

No. There will still be some premises that, because of Government restrictions, will not be allowed to operate after the 31 July. It would be unreasonable for Retailers to attempt to collect charges from these premises to cover wholesale charges when it is clear the business premise is shut and cannot generate any income. The guidance will need to be changed to reflect these remaining sectors

Certain areas may also be subject to local lockdowns similar to Leicester. If this occurs after the 31 July these premises would not be able to take advantage of a suspension of charges whereas if it had happened prior to the 31 July they would have been able to. This does not appear to protect these customers. There are sufficient checks and balances around the use of the temporary vacancy flag and the numbers should be sufficiently low after the 31 July that Wholesalers and MOSL should be able to easily spot and challenge Retailers over the use of this flag post 31 July.

- 7. Do you agree that in the event of (1): reduced consumption, and/or (2) any local lockdowns, Retailers should seek to obtain meter reads to reflect actual consumption in the market (or in the event a meter read cannot be obtained engage with customers to obtain an accurate estimate of consumption (YVE))? Please explain your answer and provide supporting evidence wherever appropriate. If you do not agree, please set out an alternative proposal.**

- (1) In the event of reduced consumption, Retailers should seek to obtain meter reads as this will always provide the truth with regards to what is happening in the market. Retailers want more than anything to have meter reads as this is the basis for accurate billing, reflective cost of sales through settlement and bills based on a read deliver better customer satisfaction. It should also be the priority for Wholesalers. Meter reads in CMOS will give them certainty around their income.

We need to move away from meter readings belonging to individual Trading Parties as everyone benefits from meter reads so it should be incumbent on all Trading Parties to input them into CMOS.

- (2) In a lockdown situation it would be very difficult to get meter reads and get in contact with customers. A temporary lockdown vacancy flag would be more beneficial and probably less costly to implement than trying to contact hundreds of premises to ascertain their YVE. PWS can contact c50 customers a day per agent without disrupting other activities. Please note, if a property is closed they are unlikely to be in the premises and so a no answer is considered as vacant

- 8. Do you agree that following the expiration of the temporary vacancy flag Retailers will have until the end of September to remove these flags from CMOS? Please explain your answer and provide supporting evidence wherever appropriate.**

Yes. We agree that there should be a period of time for customers to contact Retailers to inform them of their re-occupation. There is also a period of time required for Retailers to unwind their assumptions and undertake the necessary checks to confirm the actual date of occupancy. However, the end of September should only be a backstop date for removing the temporary vacancy flag in CMOS as it should be the aim to remove this as close to the re-occupation date as possible to ensure CMOS reflects the true market.

9. Do you agree that a new MPS should be introduced from 1 October that focusses on the timely removal of all temporary vacancy flags? If so, what are your views about how this standard should be designed? Please explain your answer and provide supporting evidence wherever appropriate.

We agree that there should be a finite time for premises to have a temporary vacancy flag in CMOS. However, it is not as simple as having a single date upon which an MPS charge can then be applied. As previously mentioned there may be localised lockdowns, premises that still cannot be opened due to legislation, the risk of a second wave etc. The numbers should however be significantly low by the 1 October and if any Trading Party is blatantly not re-occupying premises that have opened, Ofwat and MOSL should use their powers and sanctions to ensure the market is protected.

10. Do you agree that an additional MPS (or alternatively an API) should be introduced to monitor the use of YVEs in the market and incentivise the submission of more accurate consumption data? Please explain your answer and provide supporting evidence wherever appropriate.

The use of an additional MPS to monitor YVE's is fraught with danger. Any use of YVE for a post lockdown scenario is subject to assumptions whether either from the Customer, the Retailer, or the Wholesaler. A YVE will always be an estimate and to potentially charge a Retailer for an inaccurate YVE in the absence of a meter read is unfair. As previously mentioned it is in the interest of all parties to have a meter read and co-operation in achieving this will be far more preferential than designing another MPS charge.

11. If we were to introduce a financial incentive on YVEs, how could arbitrarily low YVEs entered into CMOS be identified in a proportionate way (for example via one or more simple rules)? If we were to introduce a reputational incentive on the use of YVEs, how could such a reputational incentive be strengthened?

As above any YVE is an assumption based on albeit some known facts. It will however only ever be an assumption. You could devise a hierarchy of facts to ascertain the value of the YVE along the lines of

- Customer informs Retailer of expected annual use
- Customer Business type/SIC code
- Number of employees
- Reduction in employees since resumption of business

A Retailer may carry out all these type of checks and all could lead to a wrong answer. If a customer informs a Retailer of a wrong YVE it would be wrong for the Retailer to be impacted by this in terms of MPS or any other financial incentive when it acted properly by trying to get an accurate YVE from a customer. Ofwat and MOSL should continue to monitor the use of YVE's and identify any miss-use and sanction accordingly. At the same time Wholesalers should do everything they can to ensure meters are read whether this means by supplying reads to the market, ensuring meters can be read safely by exchanging them or relocating them or by installing AMR's. Ultimately the risk of low YVE's impacts Wholesalers in the absence of a read. The incentive should be on all parties to make meter reading easier and more regular.

12. What are your views on how we can better (financially or reputationally) incentivise Wholesalers to work constructively with Retailers during the unwinding of the temporary vacancy flag and to improve the accuracy of data in CMOS?

Key to this is getting meter reading into the market. Fundamentally the meter is the wholesaler's asset and they are best placed to deliver cyclical reads as part of their normal meter reading activity. They did this in the past and a number are providing the service to the NHH market.

The responsibility for cyclical reads can be reverted to the Wholesaler and the market could design a mechanism that rewards wholesalers for submitting accurate and timely reads. To fund this Retailers would pay MOSL for access to the reads and MOSL would pay wholesalers for the read submission with an accuracy and timeliness “at risk” element to the payment.

Vacancy Flag

13. Do you agree with the expectations set out above, which will guide trading parties through the unwinding of the temporary vacancy flag?

Yes. This has been a significant situation for all parties including customers. The tail of this pandemic will be a long one and decisions made in the midst of the pandemic may prove to be wrong. There will be significant operational challenges to come especially surrounding leakage within empty premises associated with lack of meter reads and Wholesalers and Retailers must work constructively together.

Leakage policies were written for a pre-Covid period and we all need to work together to ensure an impacted customer is not further punished by adhering to pre-pandemic policies.

Market Performance Charges

14. Should Market Performance charges come back into effect from end September 2020 or end October 2020? Please explain your answer and provide supporting evidence wherever appropriate.

We don't believe an arbitrary date is particularly useful but recognise that normality must return and if this is the case October seems more sensible. No one really knows what the “new normal” will look like and gaining meter reads might be even more problematic in the near future. Buildings may remain shut and access to internal meters become impossible.

For a Retailer the meter reading MPS charges can be significant and some of the inability to access reads may not be down to the Retailer especially if the NHH world is significantly different after October to what it was in February before the pandemic.

Therefore, factors to consider are access limitations and the main meter read providers, wholesalers, may have justifiable social distancing restrictions on their field staff that prevent meters being read.

15. Should OPS charges be introduced before MPS charges? Please explain your answer and provide supporting evidence wherever appropriate.

For balance, the world might also be significantly different for Wholesalers in the “new normal” world. However, the majority of OPS work is predominately dominated by more Health and Safety concerns that can be mitigated by Wholesalers. Access issues for works that require Wholesalers to enter customer buildings may be an issue but this should not prevent Wholesalers coming up with innovative methods to remove their assets from customers buildings. Long unread meters would reduce dramatically if meters were moved to locations that didn't need customer interactions and therefore this could be seen as an opportunity.

16. Should non meter reading MPF charges come into effect before meter reading MPF charges? Please explain your answer and provide supporting evidence wherever appropriate.

Yes, as detailed above, the major factor affecting performance will be the meter reading activities.

Credit Support Requirements

17. Of the 3 options identified in relation to credit security requirements, which option do you support and why? Please explain your answer and provide supporting evidence wherever appropriate. Which option is most compatible with furthering customers interests and why?

Similar to the questions around the deferral scheme the options do not impact us as we are subject to a Parent Company Guarantee. However, we do believe that as the number of temporary vacant flags are reduced the risk to Wholesalers has significantly reduced and the fairest option is Option 1. It does not seem right that a Retailer should provide credit support for figures that are not due.

Customer Protection Code of Practice

18. Do you agree that the CPCoP does not require amendment in light of the proposals set out in this document? Please explain your answer and provide supporting evidence wherever appropriate.

We believe that although the current CPCoP is sufficient, confirmation is required that ending the use of temporary vacancy flags means that all customers are therefore not Covid affected. Although these customers may be eligible for retailer repayment schemes they may also be liable for late payment fees, interest or disconnection.

Confidential

Questions asked on behalf of the Panel, as input into Code change CPW100

- A1. What are the benefits and risks associated with implementing different credit support requirements for Retailers who have and have not deferred wholesale charges?**

[Redacted]

[Redacted]

[Redacted]

- A2. What assumptions are you making about the level and speed of return of NHH water consumption?**

[Redacted]

- A3. Please explain the makeup of your credit support and levels of Unsecured Credit Allowances in the pro-forma on the following page.**



- A4. Please tell us how regularly you reduce or increase credit lodged to match falls and rises in the P1 Settlement Report and explain what the associated costs are. Please also clearly state the monthly cost or saving you would expect to incur across your portfolio as a result of maintaining credit equivalent to July P1 vs credit equivalent to March P1 and provide supporting evidence where necessary.**

