Covid-19 and the business retail market – Consultation

Southern Water Response July 2020

Please find Southern Water's responses to both the Ofwat consultation questions and those asked on behalf of the Panel relating to Code change CPW100.

Consultation questions

Consultation question 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?

We completely agree that, for the reasons set out in the consultation, extending liquidity support in its current form (option 3) is not appropriate or necessary to support the market. An extension would increase the total amount of liquidity provided by wholesalers (an emergency short term solution) when alternative sources of liquidity are available i.e. government CBILS loans, etc. Such an extension also appears unnecessary considering the take up of the arrangements has been limited, and the coronavirus restriction are now being relaxed, with most businesses returning to some form of trading.

We would support option 1 or option 2.With option 2 assuming additional retailers are not allowed to opt in (see our response to question 3) and the deferred amounts are capped at the proposed 25% level (see our response to question 2).

We agree that the interest payable by Retailers would be applicable should the scheme be extended. For the avoidance of doubt, the interest arrangements should continue until all of the deferred amounts have been repaid in full, and therefore, the interest charges would also be applicable should option 1, to close the scheme, be implemented.

Consultation question 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.

We believe that the existing capped amount could be reduced to a lower level with little or no impact to retailers or the stability of the market. Our view is based on the limited up take of the current liquidity support scheme (only eight retailers, four of which are associated to wholesalers) and the level of deferred payments (which are substantially above the 'Deferral Floor Percentage'). We would suggest a level of 25% (75% Deferral Floor Percentage) would be appropriate, as this would still be in excess of all but one of the current retailers' deferred amounts.

Consultation question 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.

We believe that the scheme should be closed for retailers to opt into from the end of July. Southern Water has been supportive of the scheme as a temporary short term arrangement to protect business customers and the stability of the market. Retailers have now had time to secure alternative sources of liquidity and have access to government loan schemes, and therefore the arrangements should be unwound rather than extended.

We suggest that the 'Deferral Floor Percentage' would be the mechanism to implement a cap, with the maximum deferral percentage decreased to 25%.

Consultation question 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?

We support option 3, in which Ofwat would specify a back stop repayment profile for the industry. This option ensures a clear and transparent minimum unwinding of the liquidity support, which would remove any uncertainty and ambiguity for all trading parties. We believe this would be in the best interest of the market as a whole and, therefore, would ensure the stability of the market for business customers, whilst also ensuring there is no unfair competitive advantage resulting from differing repayment arrangements.

With a back stop repayment there would be nothing to deter retailers making voluntary payments above the minimum repayment requirements, as is currently available.

We oppose option 1, which we believe will create level playing field issues across the industry. It would also fail to provide sufficient certainty of the repayment profile, and could increase wholesaler exposure and risk.

Consultation question 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.

We believe that the repayment profile proposed is reasonable for all parties. Alternatively, it may be advantageous for repayments to be linear and over a longer period of time, for instance 33% repaid in October, 33% in December, and the final 33% repayment by the end of February 2020.

Consultation question 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.

We entirely agree with the proposal for the temporary Covid-19 vacancy flag to expire at the end of July. The easing of the lockdown has allowed most businesses to reopen, albeit many at a lower capacity, and the latest Government announcement will allow gyms, nail salons, tattooists, indoor pools and leisure centres to reopen in England from 25 July. Given that nearly all businesses will be allowed to reopen from the end of July it would appear that the temporary vacancy flag is no longer appropriate from August onwards.

Consultation question 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.

We understand that there may be temporary local lock-downs and restrictions, and that many businesses will be operating at a lower capacity. For these circumstances, we agree with the proposal that retailers should attempt to provide a meter reading, and where that is not possible, a customer read. Only following

failure to obtain a meter read, should the retailer engage with the customer to understand the level of reduced consumption and modify the YVE value in CMOS.

Consultation question 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.

We agree with the proposal that retailers should have until the end of September to remove all temporary vacancy flags, allowing sufficient time to obtain a meter read or update the YVE where appropriate. We would hope that retailers have continued to liaise with their customers and have already removed temporary vacancy flags where businesses have returned to trading. However, we would expect that the occupied status of all such premises would be back dated to the time the business returned to trading, which in most cases will be prior to the end of July.

From August, we would expect retailers to the use the conventional process (CSD 0104) to apply vacancy status for businesses that closed during the restrictions and have ceased trading.

Consultation question 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.

Yes, we believe that all temporary flags should be removed by the end of September and that failure to complete this task should invoke an MPS incentive. We agree with the illustrative MPS measure provided.

Consultation question 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.

Due to the adverse impacts on settlement of the inappropriate use of low YVEs we are supportive of some form of incentive. As a first stage we would suggest an API, rather than a direct MPS financial penalty, with financial penalties introduced subsequently if required.

Consultation question 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?

We would suggest an API based on the percentage of meters with YVE values below a set threshold. The value could be determined by analysis of the market data set and outliers readily identified.

Consultation question 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?

Southern Water fully supports the aim of unwinding the temporary vacancy flag as soon as possible. While the primary responsibility for achieving this is with retailers', we are committed to facilitate and to work with retailers to provide information where available, such as information on consumption where a premises has been set to vacant. However, we do not believe it is the responsibility of wholesalers to provide evidence and prove that a property is vacant, and do not believe there is a need for a specific new wholesaler incentive.

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

Yes, we fully support the expectations set out to facilitate the unwinding of the temporary vacancy flag.

Consultation question 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.

Due to the impact of the coronavirus restrictions on market activities and the resulting back log, we support a return of market performance charges in October 2020 in order to provide a sufficient time to return to business as usual.

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

No, there are similar issues in relation to operational activities, including that of key worker safety and entry to premises that have impacted operational performance. Therefore, we suggest a similar timeframe to return to business as usual for operational activities and performance charges.

Consultation question 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.

For simplicity, we would suggest that the same timeframe is used to return to business as usual and that all charges come into effect at the same time.

Consultation question 17: Note – responses to this question will be shared with MOSL. 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?

We agree that option 2 (to maintain credit support requirements at March 2020 levels until all the temporary vacancy flags are switched off) is the most appropriate. Whilst we accept that it is important that capital is not tied up in the market unnecessarily, the levels should not be reduced until the temporary liquidity measures are unwound and wholesalers increased risk is removed. Therefore, we would expect the maintenance of credit support at March levels until all temporary vacancy flags have been switched off, which may not be at the end of September for all retailers.

We also believe that the requirement to maintain the credit support at March 2020 applies to those retailers who have opted into the liquidity support scheme until all deferred amounts have been repaid. This provides wholesalers with an appropriate level of credit support until the credit risk has been reduced.

Consultation question 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.

No comment (retailer question).

[redacted]

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]

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.

[redacted]

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.

[redacted]