

April 2021

Protecting customer credit balances in the business retail market – a call for information

About this document

In April 2017, the business retail market opened which enables businesses, charities and public sector organisations in England to buy water and sewerage services from retailers, rather than their regional water and/or sewerage companies. To enable the opening of the market, changes were made to the Water Industry Act 1991 which included a requirement for Ofwat to issue, amongst other things, an Interim Supply Code.¹ The Interim Supply Code sets out arrangements to address circumstances where a retailer is no longer able to provide retail services to its customers, for example where it has exited the market due to insolvency. Where this happens, Ofwat will transfer affected customers at relevant premises to an alternative retailer to ensure continuity of retail services (an 'interim supply event').

To date, there have been two retailers² who have exited the business retail market and Ofwat has been required to use its powers under the Interim Supply Code to transfer affected customers. While market entry and exit can be a sign of a well-functioning market, these interim supply events have highlighted concerns about whether customers have an appropriate level of awareness of the risk to their credit balances held by retailers, including for example credit on account for the pre-payment of services and deposits.

We held a workshop with retailers and CCW in October 2019 to explore potential options for protecting customer credit balances. Due to the impacts of Covid-19, we were forced to pause work on this issue. However, we are now keen to resume this work in collaboration with stakeholders.

This call for information therefore seeks views from stakeholders about the current arrangements for protecting customer money held by retailers in the business retail market. In particular, we are seeking stakeholders' views on whether it would be appropriate to consider introducing measures to better protect customers. Such measures might range from periodically providing information to customers to make them aware that such credit is normally held on an unsecured basis through to considering the merits of some form of scheme to protect customer balances in the case of a retailer becoming insolvent and exiting the market.

¹ Interim Supply Code, Ofwat, September 2020 <https://www.ofwat.gov.uk/publication/interim-supply-code/>

² Aquaflo in 2019 and Tor Water in 2020

Responding to this call for information

We would welcome any comments on this document. Please email them to CPCOPcodechange@ofwat.gov.uk with the subject 'Customer credit CFI'. We are currently unable to receive responses by post.

The closing date for this call for information is **5pm Friday 30 April 2021**. If you wish to discuss any aspect of this document, please contact us by email at CPCOPcodechange@ofwat.gov.uk.

We intend to publish responses to this call for information on our website at www.ofwat.gov.uk. Subject to the following, by providing a response you are deemed to consent to its publication.

If you think that any of the information in your response should not be disclosed (for example, because you consider it to be commercially sensitive), an automatic or generalised confidentiality disclaimer will not, of itself, be regarded as sufficient. You should identify specific information and explain in each case why it should not be disclosed, which we will consider when deciding what information to publish. At a minimum, we would expect to publish the name of all organisations that provide a written response, even where there are legitimate reasons why the contents of those written responses remain confidential.

In relation to personal data, you have the right to object to our publication of the personal information that you disclose to us in submitting your response (for example, your name or contact details). If you do not want us to publish specific personal information that would enable you to be identified, our Privacy Policy explains the basis on which you can object to its processing and provides further information on how we process personal data.

In addition to our ability to disclose information pursuant to the Water Industry Act 1991, information provided in response to this call for information, including personal data, may be published or disclosed in accordance with legislation on access to information – primarily the Freedom of Information Act 2000 (FoIA), the Environmental Information Regulations 2004 (EIR) and applicable data protection laws.

Please be aware that, under the FoIA and the EIR, there are statutory Codes of Practice' which deal, among other things, with obligations of confidence. If we receive a request for disclosure of information which you have asked us not to disclose, we will take full account of your explanation, but we cannot give an assurance that we can maintain confidentiality in all circumstances.

Contents

1. Context	4
2. Possible remedies	6
3. Call for information – questions for stakeholders	9
4. Next steps	11

1. Context

In the event of a disorderly retailer exit and insolvency, customer credit balances that are due to non-household customers in the business retail market may be at risk of being partially or wholly forfeited as there is currently no mechanism in place to ensure the recovery (partially or otherwise) of this money. This risks not only customers' money, but also risks lowering consumer confidence in the market. Consistent with our strategy,³ in which we set out our aim to continue focusing our attention on markets, where they can bring the biggest benefits to customers, we are considering if there is a case for strengthening protections for customers from the detrimental consequences of a retailer failure event.

We know from our own research⁴ that just over 40% of customers are still unaware that they have a choice of retailer (and are therefore unaware of the existence of the market) and that the majority of such customers are smaller businesses.⁵ We also know that the majority of customers have not engaged with the market, either through switching their retailer or through seeking to renegotiate terms with their existing retailer, with again smaller businesses disproportionately over-represented in this group.⁶ Coupled with a lack of awareness of insolvency law⁷, we have concerns that a number of customers may be not be aware that any pre-payments or credit balances retailers hold may be at risk in the event of that retailer becoming insolvent. Customers may further be unaware that this risk could be mitigated by negotiating alternative terms and conditions with their current retailer or by switching to an alternative retailer.

We have therefore formed the following possible hypothesis:

In the business retail market a number of customers are unknowingly placing their money at risk and consequently are not taking appropriate mitigating actions to protect it.

We want to explore further the extent to which this hypothesis may be valid or indeed whether an alternative hypothesis better reflects the realities of the market at present. We

³ Time to act, together: Ofwat's strategy, Ofwat, October 2019 <https://www.ofwat.gov.uk/publication/time-to-act-together-ofwats-strategy/>

⁴ State of the Market 2019–2020, Ofwat, August 2020 https://www.ofwat.gov.uk/wp-content/uploads/2020/08/State-of-the-market-2019_20.pdf

⁵ 86% of business customers are companies with between 0–9 employees.

⁶ The Retail Exit Code (REC) provides default protection to customers who have not actively selected their water supplier in areas where the incumbent has exited the market. This includes both price protection and protection of non-price terms. See: Future protections for business retail customers: Decision on Retail Exit Code – non-price protections, Ofwat, July 2019 <https://www.ofwat.gov.uk/wp-content/uploads/2018/12/REC-Non-Price-Protections-FINAL-Decision-Document.pdf>

⁷ See “Consumer Prepayments on Retailer Insolvency”, Law Commission, 2016, paragraphs 4.2 to 4.9 <https://s3-eu-west-2.amazonaws.com/lawcom-prod-storage-11jsxou24uy7q/uploads/2016/07/56284-Law-Comm-HC-543-Web-pdf.pdf>

are mindful that there are gaps in our knowledge, which is why we are issuing this call for information to help us fill these gaps. In particular, we are keen to understand:

- The scope for generating robust data around the number of customers with some form of advanced payment tariff or who otherwise have unsecured money held by retailers. We also wish to understand the volume of customer credit that may be at risk that retailers hold.
- The policies that retailers have in place in respect of requiring customers to pay in advance or otherwise lodge credit with them and the extent to which customers are made aware of their option to negotiate alternative terms and conditions.
- The information that retailers routinely provide customers in relation to the risk to customers' credit balances in circumstances such as retailer insolvency.
- The policies that retailers have in place around the return of credit balances when customers close their account (either because they have switched to another retailer or the account is closed for other reasons).
- The extent to which issues around the volume of customer credit balances and the availability and reliability of data about this may influence the willingness and/or approach of retailers when considering whether to opt-in to the interim supply process.

We have set out specific questions that we would like responses to in Chapter 3, which cover the points above and the possible remedies that we might consider (which are set out in Chapter 2). We welcome views from all stakeholders. When responding, we would particularly welcome submissions from retailers that include data and examples of literature they provide to customers to allow us to make a fuller assessment.

2. Possible remedies

We will not introduce any changes until we have received and analysed information from responses to allow us to consider whether any changes are justified. However, it may be helpful for stakeholders to understand the range of remedies that we think might be appropriate to address our hypothesis and those in particular that we are minded to take forward in the immediate term. These remedies are not mutually exclusive and could be used individually or in combination.

2.1 Increasing customer awareness

If customers lack awareness that their money is at risk, it follows that one approach might be to take action to increase their level of awareness and allow them to make an informed choice. Communication with customers is a core function for retailers. We might therefore consider some form of requirement for retailers to set out clear statements on the risks arising from pre-payments in their communications with customers, for example on bills, and to make clear to customers the alternative options available to them.

This is a remedy which we are currently minded to introduce, unless there is sufficient evidence that it is unnecessary. Our current thinking is that this would be via a change to the Customer Protection Code of Practice.

2.2 Increased data monitoring

We have issued a number of retailer requests for information (RFIs) in the last year and some of these have required data around customer credit balances. However, we have concerns around the consistency of the data we have received. We may therefore consider introducing a regular data reporting requirement with more clarity around definitions of the data items that we require. We may also seek more detailed data than we have previously requested. We might also consider the publication of this data in some form. The intention of this remedy would be to bring greater clarity around the amount and form of customer credit held by retailers to ensure a focus on its proper management. It would also increase our ability to monitor any potential customer detriment and would increase market awareness of the issue.

This is a remedy which we are currently minded to introduce, unless there is sufficient evidence that it is unnecessary.

2.3 Changes to regulations to ensure fair treatment

Currently there is no requirement for retailers to limit the amount of customer credit that they hold. There is also not a specific requirement for retailers to proactively refund customer credit balances upon the closure of a customer's account.

In cases where retailers are holding significant levels of credit from existing customers, there might be a case to consider some form of limit on the amount of credit held. This could either be for all customers, or restricted to customers protected under the Retail Exit Code. Before considering such a remedy, we would need to be mindful of the reasons retailers have for holding customer credit and whether introducing such a remedy to address this would be justifiable and proportionate. We would also need to be mindful of the potential for unintended consequences that such a remedy might bring about.

In cases where retailers are found to be routinely holding significant levels of credit from former customers, there might be a case to introduce an obligation to return a customer's credit balance upon the closure of the customer's account. Any remedy would need to account for reasonable exceptions, such as where the customer itself has ceased trading and cannot be traced.

These are remedies which we may consider further if there is sufficient evidence of customer detriment.

2.4 Forms of insurance

In the event of a disorderly retailer exit and insolvency, customers are considered to be unsecured creditors under insolvency law and any credit balances they have are likely to be largely or wholly forfeited. Under the existing interim supply arrangements, we have the ability under the 'Offers process' to invite retailers to consider honouring the credit balances of customers that they acquire. However, there is no obligation for them to do so. It is reasonable to assume that the larger such balances are, the less motivation there is for incoming suppliers to honour them as it may make the acquisition of the customers uneconomic. For this reason, introducing a requirement on retailers seeking to acquire customers in interim supply to honour customer credit balances is likely to prove counter-productive and dissuade retailers from participating.

There are a number of possible approaches that might provide some form of insurance for customers' credit balances which means that customers are not bearing a financial risk from their retailer becoming insolvent. Such approaches could include a requirement on each retailer individually to put in place a scheme to insure their customers' credit balances (for example, through placing money in a ring-fenced trust). Alternatively, there could be a requirement placed on retailers to act collectively to pool risk by all contributing to a fund which can be drawn on to reimburse customers upon a retailer's insolvency. Another

approach could be to require the payment by retailers of premiums to a third party to provide cover for customers' credit balances.

At the moment, we do not have sufficient evidence as to the costs of such insurance schemes (which are likely to be passed through to customers) or how practical they would be to introduce. Our view is that this type of remedy would only be justifiable if there was significant evidence of customer detriment that could not be remedied through lighter-touch approaches. As the costs of such schemes are likely to fall (at least in part) on to customers, there would need to be strong evidence of customer support for it.

These are remedies which we are not currently minded to introduce, but could consider if there is evidence of severe customer detriment that other remedies would be unlikely to adequately address.

3. Call for information – questions for stakeholders

In this call for information, we welcome responses from stakeholders to the questions below and welcome any further views not covered. We also welcome supporting evidence – such as relevant data sets and examples of relevant literature provided to customers.

3.1 The hypothesis

1. We set out in section 1 the following hypothesis: **In the business retail market a number of customers are unknowingly placing their money at risk and consequently are not taking appropriate mitigating actions to protect it.** What evidence do you have to help us understand whether or not this hypothesis is valid?

3.2 Retailer policies and approach

2. What policies do retailers have in place in respect of requiring customers to pay in advance or otherwise lodge credit with them?
3. How many customers are affected by each policy?
4. To what extent are customers made aware by retailers that their money may be at risk and of their option to negotiate alternative payment terms or switch to an alternative retailer?
5. To what extent do issues around the volume of customer credit balances and the availability and reliability of data about this influence the willingness and/or approach of retailers when considering whether to opt-in to the interim supply process?

3.3 Increased data monitoring

6. What specific items of data would help us test our hypothesis and how easy or difficult would it be to generate this data?

3.4 Approach to remedies

7. When considering remedies in general, is there a case for the different treatment of customers (for example depending on whether or not they have engaged in the market)?
8. Are there any remedies that we have not considered that you think we should have?

3.5 Changes to regulations

9. What views do you have on our intent to introduce a requirement on retailers to better inform customers about any credit balances being at risk and their options to mitigate this risk? How might this be most effectively implemented?
10. What views do you have on our intent to require retailers to regularly report to us on customer credit balances that they hold? Please set out (with reasons) how frequently you consider such reports should be made, and the type of data that we should collect.
11. What views do you have on the option of introducing a requirement on retailers to limit the amount of customer credit that they hold? Please set out (with reasons) the form that such a limit might take, and any risks or unintended consequences of such an approach you believe there are and how these might be mitigated.
12. What views do you have on the option of introducing a requirement on retailers to return customer credit balances upon the closure of a customer's account? Please set out (with reasons) any reasonable exceptions that there might be to this requirement and how such exceptions should be addressed.

3.6 Forms of insurance

13. We are not currently minded to consider the establishment of any form of insurance scheme. Do you agree that we should not be considering this option at this time? If you think that we should consider insurance schemes, please provide reasons and set out if there is any particular approach that you think we should consider further.

4. Next steps

We will carefully consider evidence provided by stakeholders before deciding whether any further action on our part is justified. We note the interim approach that the Water Industry Commission for Scotland (WICS) has set out in respect of the treatment of customer credit in the Scottish Business Retail Market⁸ and will also take into consideration any further measures that may be introduced in Scotland. However, as WICS notes in its consultation, there are material differences in the two market frameworks that may support the use of different measures in the respective markets.

We will publish a summary of the responses that we receive, and in the same document we will set out any further action that we intend to take and our reasons for doing so. Before introducing any remedies we would consult on any specific proposals.

⁸ COVID-19 Measures in Support of Non-household customers, WICS, May 2020
<https://www.watercommission.co.uk/UserFiles/documents/Water%20Charge%20Relief%20Scheme.pdf>

**Ofwat (The Water Services Regulation Authority)
is a non-ministerial government department.
We regulate the water sector in England and Wales.**

Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

Phone: 0121 644 7500
Fax: 0121 644 7533

© Crown copyright 2021

This publication is licensed under the terms of the Open Government Licence v3.0 except where otherwise stated. To view this licence, visit nationalarchives.gov.uk/doc/open-government-licence/version/3.

Where we have identified any third party copyright information, you will need to obtain permission from the copyright holders concerned.

This document is also available from our website at www.ofwat.gov.uk.

Any enquiries regarding this publication should be sent to mailbox@ofwat.gov.uk.

OGL