Market Arrangements Code/Wholesale Retail Code Change Proposal – CPM048/CPW131

Modification proposal	Market Arrangements Code/Wholesale Retail Code Change Proposal – CPM048/CPW131 – Suspending certain MPS charges pending full review of the MPF
Decision	The Authority has decided to reject this Change Proposal
Publication date	19 October 2022

We are rejecting this Change Proposal.

We consider that there is significant potential for customer detriment to arise as a result of suspending these market performance standards charges in their entirety. There is a risk that suspension of all charges for MPS 17, 18 and 19 would lead to reduced incentives on and effort by Retailers to obtain actual meter reads, leading to poor customer outcomes and potential missed opportunities to identify and address leakage. The proposed solution also potentially erodes the incentive for Retailers to engage with Wholesalers to improve asset and data quality issues.

We do, however, think that there is potential to significantly improve the incentives on Trading Parties to, amongst other things, bring about further improvements in areas such as data quality. MOSL is working with market participants (including Ofwat) to design appropriate incentives, through reform of the Market Performance Framework (MPF). We see progress on MPF reform as a key priority for improving market functioning, in particular improving data quality and Trading Party performance.

While we do not consider that the evidence presented in support of this Change Proposal forms a strong enough case to justify the suspension of these charges in their entirety, MPF reform provides an opportunity to develop a performance framework which effectively incentivises both Wholesalers and Retailers to improve specific aspects of their performance and deliver better service to business customers in the market. We believe the information gathered as part of developing this Change Proposal can be a useful input into the design of the enduring MPF.

Background

CSD002

Wholesale Retail Code Subsidiary Document CSD 0002 (Market Performance Framework) sets out various processes and incentives designed to support standards of performance by Trading Parties against their obligations. This includes Market Performance Standards (MPS) where Retailers and Wholesalers are charged for underperformance against these standards. The Market Arrangements Code (MAC) sets out the mechanism for collection of these charges.

CSD 0002 includes requirements for Retailers to take transfer, twice-yearly and monthly meter reads within prescribed timescales. MPS 18 (twice-yearly read meters) and MPS 19 (monthly read meters) currently permit five percent (5%) of tasks to breach the success criteria or time parameter before charges are incurred, recognising that there may be circumstances where the Retailer is unable to read meters due to issues outside their direct control.

MPF Reform

The Market Operator, with the support of the Strategic Panel and Ofwat, has established a programme to carry out a root and branch review of the MPF. This follows on from a review of the MPF, commissioned by the Market Performance Committee (MPC) in 2019. This review concluded that the MPF was lacking in data, transparency, accountability and customer focus, in particular:

- The MPF is not linked to customer outcomes
- Targets are not stretching
- Performance lacks 'public profile'.

Towards the end of 2021 a Call for Inputs was issued to stakeholders, along with the appointment of a delivery partner and the definition of a two-phase programme of work to review the MPF. Phase 1 of the programme is identifying the risks and issues that prevent the market delivering on its desired outcomes, as well as the activities that could enable the delivery of these outcomes as part of a future MPF. MOSL has recently published a consultation seeking feedback on the work done by the programme so far. It will also identify the types of interventions that could form part of a reformed MPF by January 2023. Phase two will comprise the detailed design and implementation of the preferred MPF model, including the development of specific measures, performance standards, and associated incentive mechanisms, as required. This phase is expected to run through 2023 and 2024.

MPS Charges

MPS charges are capped at 0.25% of the R1 settlement charges (see section 3.4.2 in CSD 0002). The total capped MPS charges invoiced to Retailers averaged £250,000 per month for the period April 2021 to December 2021[1]). MPS 17, 18 and 19 together make up 99% of the total MPS charges invoiced. MPS and Operational Performance Standard (OPS) charges collected may be used by the Strategic Panel to fund Market Improvement Fund (MIF) projects. If the MPS and OPS charges are not utilised through the MIF, they are redistributed back to Trading Parties in an incentive-neutral manner.

The issue

As already explained, Market Performance Standards 17, 18 and 19 relate to Retailers taking meter reads within specific timescales. There are circumstances when it may not be possible for Retailers to obtain a meter read due to factors outside the Retailer's control. Factors cited include customer issues (for example, customers denying access to the meter) or Wholesaler issues (for example wrong/missing meter data on CMOS). Consequently, the Proposer believes that it is unsound to charge Retailers for MPS 17, 18 and 19.

The Change Proposal[2]

This Change Proposal was raised by Castle Water Ltd on 3 December 2021.

The change seeks to suspend charging for MPS standards 17, 18 and 19 until a new MPF is implemented following the MPF reform programme. This involves suspending the requirement for the Market Operator to issue invoices on, and Retailers to pay, MPS 17, 18 and 19 charges.

The proposed implementation date of the change is 29 November 2022.

---

[1] MPS charges were temporarily suspended between March 2020 – March 2021 in light of Covid-19 restrictions

[2] The change proposal and accompanying documentation is available on the MOSL website at https://www.mosl.co.uk/market-codes/change#scroll-track-a-change

A Post Implementation Review (PIR) is proposed to take place six months after implementation. The PIR will compare the performance trends of MPS 17, 18 and 19 before and after CPM048/CPW131 are implemented. The PIR is proposed to use only six months of data as the MPF Reform is expected to be implemented during financial year 2023/24.

Industry consultation and assessment

A consultation was held between 15 February and 8 March 2022. There were 21 respondents (11 Retailers, nine Wholesalers and the Consumer Council for Water (CCW)). Of the 11 Retailer respondents, seven provided qualitative responses to the consultation and four provided missed meter reading (skip code) data only.

Full responses to the consultation can be found in the Final Recommendation Report (FRR), however there were three main areas of focus:

- insight and views on the proportion of skips (missed meter readings) that are outsider Retailers' control, and the reasons for these. Most Retailer respondents thought that 50% of skips were outside their control, with the main reasons being inability to gain access, incorrect location information and asset issues such as flooded meter chambers.
- views on whether or not Retailer MPS charges provide an incentive to read meters. Opinions on this were divided, with 4 Retailers stating that MPS charges have little or no influence, and 3 others citing a high influence.
- The potential impact on customers from removing MPS17/18/19 charges. Again, there were very mixed responses. Some thought that there would be no impact, while others thought there was potential for high impact. Respondents expressed concern about incentivising the right Retailer behaviour and wider market impacts that could arise should fewer actual meter readings be obtained.

Four areas of analysis (methodologies) were employed by the Market Operator (MOSL) to assess the case for change:

1. analyse the overall trend in MPS performance over time

2. understand the reasons why meters could not be read (or were 'skipped') by collecting skip code data from Retailers

3. investigate CMOS data to understand the volume of instances where there is not a substantive opportunity for the Retailers to read the meter before the charge is incurred

4. consult on a range of questions to provide qualitative response to the change.

Methodology 1: The trend of the percentage of meters settled on actual reads was looked at between October 2017 and February 2022. This period included the Covid-19 outbreak and while Covid-19 restrictions did not ban meter reading activities, there was an impact on Retailers' ability to read meters. Also during this period, a Code change (CPW078/CPM020)[i] was introduced that affected MPS 18 performance. The analysis showed that the percentage of meters settled using actual consumption did not significantly improve from Settlement Run R3 (eight months after the end of the Invoice Period) to Final Settlement Run RF (sixteen months after the Invoice Period). Retailers stated that they submit meter reads whenever they obtain them, regardless of the Settlement timetable.

Methodology 2: This involved collecting skip code data (i.e. the reasons why a visual meter read was not obtained) from Retailers. To facilitate the data gathering exercise, MOSL supplied a random, statistically significant sample of meter IDs that have incurred MPS 17, 18 and 19 charges to each Retailer on a confidential basis. Retailers were asked to provide their skip codes for this sample, and to group them into a small number of generic categories agreed with the Proposer. These categories were "unspecified; Retailer access; Unable to determine; Wholesaler location; Wholesaler asset; vacant Covid; Retailer asset; Skip not yet available; Vacant". The aim of the exercise was to provide a reasonable estimate of the level of charges levied across the market where the issue was considered to be outside the control of the Retailer.

From the skip code data provided, the largest category used (39.9%) was "unspecified" (i.e. little to no details provided for why the meter wasn't read). Together with the categories 'Unable to determine' and 'Skips not yet available', these represent 57.7% of the data. It should be noted that not all of these were completely devoid of data (e.g. some contained free text fields for the skip code reason), and these provided material for textual analysis. This textual analysis was helpful in indicating that Retailers had correctly used the categories, and in providing more detail about the issues encountered.

The second largest category of skip code (17.1%) submitted by retailers was 'Retailer access', which corresponded with the qualitative answers provided by Retailers in consultation responses. Examples of 'Retailer access' issues include customers denying access and access is obstructed.

The Final Recommendation Report (FRR) explains that determining the share of performance failures outside the control of Retailers is heavily dependent on the treatment of the skip codes in the sample which were either missing usable information or where the information was insufficient to enable mapping to one of the specific reason categories. This translates to a significant 4,186 (49.1%) of the performance charges in the sample. It is also not straightforward to resolve as it is not known whether these skips were random.

From the analysis carried out, and based on the responses from Retailers, MOSL estimates that 36-40% of performance failures appear to be for reasons outside Retailer control. This estimation is disputed by the Proposer, who considers that the evidence gathered suggests that significantly more than half of all skips are outside of the control of a Retailer.

Methodology 3: MOSL examined the CMOS data set to assess the materiality of scenarios where there was not a substantive opportunity for the Retailers to read the meter before the relevant MPS charge was incurred (for example, when a meter should have been removed from the market, or details updated by the Wholesaler). The number of tasks caught by these scenarios represented 0.3% of MPS 17, 18 and 19 tasks, and 2.1% of fails for the three standards across the period. The total attributable charge equates to £47,283.71 after application of the MPS charge cap which represents 2.1% of total MPS charges collected across this period. This analysis shows that there are scenarios where the meters should have been removed from the market (therefore avoiding becoming a MPS task) and/or had their details updated so that Retailers have a reasonable opportunity to read them. However, such cases are limited.

Methodology 4: consultation with the industry for qualitative responses on why they failed to read the meters in time, and what are the likely operational and customer impacts should MPS 17, 18 and 19 charges be suspended. Of the seven Retailers who provided a qualitative response to the consultation, six reported that half or more of the skips (failed meter reads) are outside of their control. Another Retailer stated that it only considered meter location data issues as being outside of their control.

Three Retailer respondents stated that 'Retailer Access' was their most commonly used skip code category, e.g., denied access to internal meters, meters which are temporarily inaccessible, lack of access to premises (including due to Covid-19 restrictions) and appointments needed. The second most common category across these three respondents was 'Wholesaler Location', which includes meters that have incorrect 'XY' co-ordinates and location notes, and meters that have been relocated without updating CMOS. The third most common category reported by these respondents was 'Retailer Asset' and 'Wholesaler Asset'. Retailer Asset encompasses situations where the meter chamber may be flooded and where the meter reader did not carry the correct equipment to deal with a meter. Wholesaler Asset includes cases where the meter lid is jammed, the meter has a flooded chamber as well as CMOS not being updated for meter exchange or meter removal.

Views of the Customer Representative

The consultation sought views on the expected impact on customers if this change were implemented, and whether there might be any detriment to customers' experience. The Consumer Council for Water (CCW) stated that they did not support the proposal to suspend the MPS 17, 18 and 19 charges while the MPF is under review. In 2020-21, CCW received 2,188 complaints relating to billing and charges, with over 40% of these attributable to customers disputing their measured charges. CCW highlighted that a key factor that drives dissatisfaction in this area is poor estimation, and so it is vital that Trading Parties are incentivised to take timely meter reads. If these performance charges are removed, CCW believes this will be detrimental to customers, as important incentives will be weakened.

CCW agreed that the current MPF is in need of reform, particularly as there needs to be greater incentivisation on Trading Parties to deliver good customer outcomes. However, they stated that this does not mean that existing MPS measures are not providing any such incentive to the point that it is warranted for performance charges to be suspended. Given the market-wide problem of poor data quality, CCW considers that it is important that Retailers continue to be subject to performance incentives. It is vital that meter reads are frequent and accurate to ensure customers are billed on actual usage, and to aid leakage detection efforts. Therefore, CCW stated that it is not appropriate to remove performance charges where this could worsen customer outcomes and pointed out that there is no guarantee at present that the MPF will be reformed in a way that significantly improves customer outcomes, which would therefore leave a large gap in customer protection.

CCW acknowledged that there may be situations where Retailers are unable to take meter reads due to circumstances outside their control but noted that this does not mean that a suspension of performance charges is justified. Firstly, there may be circumstances where a Retailer is directly responsible for being unable to take a read. Removing a performance charge could result in a lack of incentive to address the cause. Secondly, even in cases where the Retailer was not directly responsible, a performance charge could still act as an incentive to try and overcome the difficulties experienced in obtaining those reads (e.g. by working closer with Wholesalers and customers). Incentives are important to drive the right market behaviours and help deliver improved customer service.

CCW challenged the Proposer's assertion that a natural incentive to take meter reads exists due to customers refusing to pay bills based on estimates. CCW is aware through customer complaints that some customers challenge their charges, but this can be due to the poor quality of an estimate, rather than a problem with estimation itself. In addition, customers may be forced to settle such bills when taken through debt recovery proceedings as a means of avoiding disconnection or court action. Retailers ultimately being able to enforce estimated charges weakens the natural incentive to read meters that the Proposer suggests. It is, therefore, important that performance measures remain in place to ensure that there are incentives on Trading Parties to improve the quality of data for the benefit of customers.

While this proposal may benefit Retailers in the form of reduced performance charges, CCW stated that there is no evidence that there will be any benefits for customers. CCW considers that it will be detrimental to customer service. Therefore, CCW does not believe that this change meets the Primary Principle of the MAC Objectives & Principles, both for the lack of customer benefits, and for the reasons stated above. It is especially unclear how the removal of performance charges will result in Retailers devoting more time to addressing underlying causes of poor data quality.

The consultation asked for views on the expected impact of this change on the accuracy of customer bills and/or settlement. CCW stated that there could be a detrimental impact on billing accuracy if important incentives are removed on Retailers to regularly take and submit meter reads. In CCW's experience, customers want frequent and accurate meter readings to enable them to be billed on actual usage. If incentives to take meter readings are reduced, this could lead to a decrease in the number of actual reads being taken, thereby reducing the accuracy of customer charges. If and when charges are subsequently corrected, this could lead to customers receiving backdated bills, and bill shocks. From its complaints evidence, CCW knows that this causes financial uncertainty for affected customers and believes this could be increased as a result of this proposal.

CCW also offered these additional comments: "We agree that the on-going MPF review could benefit from the insight obtained from Trading Parties regarding the reasons why they are unable to read meters. However, there should not be an over-reliance on skip code data as the main source for insight as there may be many other cases where reads have not been obtained due to meter readers having failed to attend the site. As these reasons may not be captured as a skip code, MOSL and the Proposer should examine this area further when making the final recommendations on this change proposal."

Code Change Committee discussion and recommendation

The Code Change Committee (CCC) considered this Change Proposal at its meeting on 24 May 2022. It voted by majority to recommend that the Authority reject the proposal (one vote in favour of approval and seven votes in favour of rejection).

When discussing this change, the CCC noted it had not been possible to definitively quantify the proportion of skipped meter reads that were outside of Retailers' control due to missing or incomplete information from Retailers as to why meter reads had been skipped. However, the analysis and qualitative feedback from the consultation did present a strong case for reviewing the current incentive regime and the CCC noted the ongoing reform of the MPF to resolve this. In the meantime, many members felt the uncertainty in the analysis' findings was too great to support the case for this change.

A CCC member observed that as Retailer MPS performance increases, factors outside of the control of Retailers would account for a greater proportion of remaining MPS charges. Another member believed it would be difficult to design an incentive framework that eliminated all factors outside of Retailers' control.

The CCC accepted that a proportion of MPS charges were likely due to factors outside Retailer control, but the proposed solution also suspended the incentive for those that are under Retailer control. Therefore, the impact of removing the incentive for these also needed to be considered. The customer representative advised that 70% of customer complaints related to billing and therefore there should be an incentive to ensure accurate bills. Most members agreed that suspending MPS charges for meter reads under Retailer control would result in a worse outcome for customers. Another member considered that suspending charges would not demonstrate a progressive market and would be difficult to justify to customers.

A member said that the Market Performance Committee's (MPC) view was that MPS charges drive Trading Parties to focus on resolving issues that cause them to incur charges. The MPC considered that market performance still needed to improve and without MPS charges, Trading Party behaviour would not change to address hard-to-read meters.

The CCC asked the Proposer if they had considered alternative solutions such as amending the threshold where charges do not apply. The Proposer believed code obligations and business need to read meters were sufficient incentive to read meters and MPS charges had no further influence on this, particularly where the Retailer was waiting for Wholesaler action, and therefore they proposed to suspend the charge in full.

Our decision and reasons for our decision

We have considered the issues raised by this Change Proposal and the supporting documentation provided in the Panel's Final Report and have decided to reject the proposal as we do not consider that it facilitates the **Primary Principle**.

We disagree with the Proposer that this change would further the **Primary Principle** which seeks to protect and promote the interests of, and participation by, existing and future Non-Household Customers. We consider that there is significant potential for customer detriment to arise as a result of suspending these charges in their entirety. There is a risk that suspension of all charges for MPS 17, 18 and 19 will lead to reduced incentive on and effort by Retailers to obtain actual meter reads and could lead to an incentive instead to defer to using estimates on an ongoing basis. We consider that this could result in customer detriment, including potentially missed opportunities to identify and address leakage or to identify where the occupancy status of a property has changed. We also share CCW's concerns that removing charges for underperformance against these measures potentially undermines the incentive for Retailers to raise bilateral requests and work collaboratively with Wholesalers where asset or data quality issues are identified.

We have also considered carefully whether the implementation of this Change Proposal would facilitate any of the supporting principles under the market codes. We do not agree that this change facilitates a **seamless non household customers experience**, as it does not address any issues with differing levels of performance across Wholesaler areas. Instead, it could lead to a reduced incentive to identify and address issues that are preventing meters from being read, as explained above.

The Proposer is of the view that the change would also facilitate the **Operational Terms objectives** of the WRC, arguing that there is currently a perverse incentive on Retailers not to submit late meter reads in order to avoid incurring performance charges. We disagree that this perverse incentive exists as charges for submission of late reads were removed in 2019.

The Proposer states that Retailers' responses to the consultation support the hypothesis that a material proportion of the meter reading skips are due to factors outside of the Retailer's control, thereby rendering the basis of charging for MPS 17, 18 and 19 unsound and the purpose of "incentivisation" under the current Market Performance Framework as pointless. Whilst we note the evidence provided suggests that the current 5% allowance for events outside the Retailer's control may be insufficient, the Proposal seeks to remove the measure in its entirety. The evidence presented in the FRR suggests there are still a significant proportion of reads which are entirely within the Retailer's control or can be adequately rectified with timely intervention and communication with other market participants. There is also scope for pursuing innovative ways of obtaining meter reading data, including encouraging customers to submit their own meter readings. In addition, Retailers are protected by an overall cap on MPS charges, which limits the financial impact that could arise. The solution proposed by this Change Proposal would remove the financial incentive for Retailers to play their part in improving data quality, which is in the interests of customers.

We note that in its analysis of skip code data, MOSL questioned whether an immediate and full suspension of MPS charges was justified. They suggested that an alternative approach might be to increase the threshold below which MPS 18 and MPS 19 charges do not apply. A Wholesaler also suggested tweaking the task completion time parameters. We do not consider that the costs and benefits of these alternative solutions have been sufficiently explored and analysed. We note that the Proposer decided not to pursue these suggestions further, on the basis that they consider the framework as a whole is not fit for purpose. We do not think that this is a fair reflection of the view of industry, as captured through the views obtained as part of the consultation process. We fully support MPF reform, but whilst that work is ongoing it is our opinion that the MPF in its current form still helps to incentivise the timely completion of key market processes and is to be preferred to the option of no incentives.

In summary, we do not consider that the Proposal is based on, nor has it provided, sufficiently convincing evidence to warrant the complete suspension of these performance charges pending reform of the MPF. Whilst the analysis does suggest that some MPS underperformance may be outside the control of the Retailer, there is too much uncertainty in the skip code analysis and the Proposer places heavy emphasis on anecdotal feedback from Retailers. There is no recognition that the solution proposed would remove the financial incentive for Retailers to complete tasks that *are* within their control. It would therefore be wrong to suspend these performance measures in their entirety.

We note that the MPF review will consider these performance measures and associated interventions as part of its remit. Pending the reform of the MPF, MOSL has recently instigated a new Holistic Performance reporting methodology, which contains metrics focussing on data completeness and addressing legacy long unread meters. In addition, the introduction of more specific skip codes through implementation of CPW120 and CPW130 in May 2023 should in due course provide the market with clearer data and evidence on reasons why meters cannot be read and allow a much better understanding of the root causes for this and how these can be rectified. We consider that these code changes, along with the Holistic Performance reports, could enable

Wholesalers and Retailers to address some of the issues that are preventing the reading of meters.

The Proposer suggests that in a competitive market, Retailers have a natural incentive to gain actual meter reads where they have the ability to do so, and do not need the threat of a financial penalty to force them to do so. It is worth noting that customer awareness of, and engagement with, the market is still below 50%[3], so we cannot rely solely on market forces to protect customers' interests. We also note that market frictions, including poor quality customer, consumption and asset data continues to impede the effective functioning of the market. Trading Parties have code and licence obligations in relation to the provision and maintenance of good quality data, which they must comply with, and financial incentives can be a useful means of further incentivising compliance with these requirements.

Therefore, we do not consider that removing performance incentives in their entirety is appropriate, given the importance of good quality data based on actual meter reads which feeds through directly into customer bills. As CCW points out, poor quality estimates used in billing has been a key cause of customer complaints, and it is therefore important that performance measures remain in place to ensure that there are incentives on trading parties to maximise data quality for the benefit of customers. It should be borne in mind that customers can provide meter readings too.

We note that the Proposer referenced Ofwat's previous decision to temporarily suspend MPS charges during the Covid-19 Lockdown, arguing that this set a precedent for the removal of charges where the activity concerned is not within the Retailer's control. In the FRR, the Proposer refers to an "established principle" previously determined by Ofwat, in that "…Trading Parties are not unfairly penalised for failing to meet market performance standards due to factors outside of their direct control".

We reject this argument for two reasons. First, for the reasons given above we do not agree that the current measures unfairly penalise Trading Parties for failing to meet performance standards due to factors outside their control.

Secondly, the Proposer ignores the specific context of the temporary suspension of MPS charges during the Covid-19 Lockdown. The suspension of charging over that period was deemed to be a temporary action in recognition that many MPF measures – including in relation to meter reading – *could* be materially affected by unprecedented

---

[3] In 20/21, only 43% of business customers were aware that they have a choice of Retailer and in 21/22 - see the State of the market 2020-21: Review of the fourth year of the business retail water market - Ofwat. See also: Five Years Open for Business Review of the fifth year of the business retail water market 2021-22.

by the social distancing and business closure measures imposed to combat the outbreak of Covid-19. The position since that time has changed significantly as all legal restrictions relating to social distancing have now been lifted and the Proposer has not referred to any similar public health risks or legal measures preventing the taking of a meter read.

Decision notice

In accordance with paragraphs 6.3.7 and 7.2.9 of the Market Arrangements Code, the Authority rejects this Change Proposal.

Georgina Mills
Director, Business Retail Market

---

[i] CPW078/CPM020 Priority Performance Regime Changes: https://www.ofwat.gov.uk/publication/wholesale-retail-code-and-market-arrangement-code-change-proposals-ref-cpw078-and-cpm020/