

## Market Arrangements Code/Wholesale Retail Code Change Proposal – CPM046/CPW133

<b>Code modification proposal</b>	Market Arrangements Code/Wholesale Retail Code Change Proposal – CPM046 and CPW133 – Approved Codes of Practice
<b>Decision</b>	The Authority has decided to reject this Change Proposal
<b>Publication date</b>	08/02/2023

### We are rejecting this Change Proposal.

We do not consider that this Change Proposal, as presented, sufficiently demonstrates how the proposed Approved Codes of Practice (**ACoP**) Framework will deliver added value to business customers that cannot be realised through existing market change mechanisms. As such, we do not think that this Change Proposal furthers the Primary Principle.

However, we fully support and encourage the continued development and adoption of Retailer Wholesaler Group (**RWG**) good practice guidance by Trading Parties. We encourage Trading Parties to utilise the existing market mechanisms, where relevant, to facilitate the elevation of RWG guidance into the Codes. Recognising the benefits to Trading Parties and business customers of standardising processes across the industry, we support the elevation of good practice guidance through a greater commitment from Trading Parties to fully align with RWG guides.

In principle, we support standardised processes and policies across the market that can contribute to improving customer outcomes and reducing market frictions. However, the Proposal as presented does not sufficiently evidence what added value the introduction of the proposed ACoP framework would provide, relative to formalising RWG guidance through the existing code change mechanism.

We have also identified concerns with the Proposal, noting that the underlying ACoP assessment and amendment process has not been clearly defined. Further to this, we have reservations regarding the legal drafting proposed as part of this solution; noting that the proposed legal amendments are not consistent with how current governance arrangements are defined in the Market Arrangements Code (**MAC**), and the fundamental ACoP assessment and implementation processes are not clear within the proposed legal drafting.

## Background

This Change (the "**Proposal**"), initially raised in September 2021, intends to introduce an Approved Codes of Practice (ACoP) framework that will provide a formal route for formalising good practice guidance within the Market Codes.

Industry bodies, in particular the RWG, produce industry good practice guidance on specific issues that seek to align Trading Party policies and processes, so as to support effective and efficient market operations and functions. Within the RWG's governance framework document<sup>1</sup>, which set out the group's proposed objectives and outputs, the RWG referenced ACoPs which would 'provide a minimum standard in relation to particular areas of policy or practice in the market'. This also suggested that Trading Parties would be required to adopt ACoPs and must demonstrate that they provide a level of service which is the same as or equivalent to that set out within the ACoP.

United Utilities (the "**Proposer**") raised CPM046 on 15 September 2021, initially presenting this to the Panel at its September 2021 meeting. MOSL advised the Panel that CPM046 warranted a sub-group given the substantial assessment required.

MOSL later confirmed to the Code Change Committee (**CCC**) that a change to the Wholesale Retail Code (**WRC**) would also be required to deliver the proposed solution, therefore CPW133 was proposed alongside CPM046.

## The issue

Industry groups, including the RWG, produce good practice guides that set out detailed information to support the alignment of Trading Party processes and policies on specific issues. While guides exist to promote and share good practice across Trading Parties, they are ultimately only guidance and not mandatory. At present, good practice guides are not supported by any formal incentive or disincentive for adoption as they sit outside of the current Market Codes. Instead, Trading Parties are relied upon to recognise and adopt the guidance, meaning adoption of RWG's guides is not consistent across the market.

This variation in Wholesaler policies across the market can have a detrimental impact on Retailers and customers. The misalignment of processes contributes to cumbersome Retailer-Wholesaler interactions that in turn can result in sub-optimal outcomes for customers. The detriment to customers is expected to be heightened for multisite customers operating across multiple Wholesale regions, given the inconsistency of Trading Parties' processes.

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<sup>1</sup> See: [RWG - Governance Framework \(mosl.co.uk\)](https://www.mosl.co.uk/governance-framework)

While the Wholesale Retail Code does contain information on processes<sup>2</sup>, there are gaps within the current Codes for certain processes where the absence of no minimum or absolute standards are set. Consequently, it is suggested that supplementary information set out in the RWG guidance could be enhanced within the Codes to align Trading Party processes.

While RWG guidance can be elevated into the WRC through the existing Code change process, there is no formal route or process for assessing and converting existing RWG guides into the Market Codes. The absence of a clear governance framework means there is no path for elevating guidance for mandatory adoption by Trading Parties, contributing to the market frictions of inefficient Wholesaler-Retailer interactions, and inadequate Wholesaler performance.

## The Change Proposal

The Proposal intends to establish a framework that will enable ACoPs to be introduced within the Market Code framework through a new suite of code documents that will sit alongside the existing WRC and MAC. The intent of the Proposal is to support the formalisation of good practice guidance to ensure that the existing compliance and enforcement provisions are also applied to approved ACoPs.

By setting out detailed information in a separate suite of documents, the Proposer considers that processes will be easily and clearly accessible for Trading Parties. The Proposal also notes that this provides Trading Parties with the opportunity to notify customers of their compliance with ACoP standards, as customer-friendly language can be adopted in these documents, increasing the transparency and accessibility of information for customers.

The Proposer views the proposed ACoP framework as a more efficient approach to introducing and amending ACoP standards rather than inserting and amending clauses within the WRC through multiple Change Proposals.

It is proposed that the existing Code Change process would be followed for the assessment and development of ACoP proposals, while the compliance and enforcement mechanisms of the Market Codes will be expanded to include the obligations set out within ACoPs. Where ACoP standards have an undefined delivery method, Parties will be required to demonstrate delivery of the intended outcomes. The Proposal intends to expand the role of the Market Performance Committee (MPC), and the existing Audit process, to include reviews of performance against ACoP standards, which are expected to be captured as Additional Performance Indicators (APIs). In accordance with the existing MPC rectification route, persistent non-compliance would be escalated to Ofwat for the Authority to determine the most appropriate steps to address non-compliance.

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<sup>2</sup> The WRC Schedule 1, Part 3: Operational Terms set out the process steps to be followed in order for Trading Parties to complete operational activities, for example processes for metering.

The Proposal notes that formalised ACoPs will fall within the scope of Non-Trading Disputes, meaning these can be raised by a Party against another due to performance against ACoPs' standards.

The Final Recommendation Report<sup>3</sup> (FRR) states that RWG good practice guides will continue to exist, as the RWG may produce guides that are beneficial for the market. If the Proposal is implemented, the RWG will consider whether elements of these guides should be elevated to the mandatory status of ACoPs.

## Industry consultation

The industry consultation for CPM046 and CPW133 was conducted between 21 March 2022 and 8 April 2022. 16 responses were received from industry: six Retailers, nine Wholesalers, and the customer representative, the Consumer Council for Water (CCW). Responses to the industry consultation are available on the MOSL website<sup>4</sup>.

This section outlines the key points raised in consultation responses, and the responses provided by the Proposer.

### Recognition of the benefits

Twelve respondents agreed with the intent of ACoPs to improve customer outcomes, noting that formalising content from RWG guides improves clarity and consistency across the market. The majority of respondents also agreed that the elevation of ACoPs within the Codes should benefit end customers through greater consistency across the market that ultimately improves the efficiency of Wholesaler-Retailer interactions.

### ACoP assessment process needs to be defined clearly

Some respondents questioned whether the introduction of the ACoP framework is the most appropriate way to address inconsistencies across Wholesalers' processes with RWG good practice. One response noted that standardisation of processes was not appropriate given the variation in Wholesaler business models and operations, in part due to geographical differences. Similarly, seven respondents expressed the view that a robust and detailed assessment of a proposed ACoP needs to be outlined within the ACoP framework in order to consider the full impact of an ACoP on stakeholders. Three respondents also noted that the approval process should consider whether the benefits of standardisation come at the expense of innovation in the market. The Proposer notes that formalising ACoPs within the Market Codes will have an impact on Trading Parties; however, the costs and benefits of a proposed ACoP would be considered as part of the assessment process' cost and impact analysis to determine the net impact of an ACoP.. The Proposal indicates that the assessment

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<sup>3</sup> See: [Approved Codes of Practice - Recommendation \(mosl.co.uk\)](https://www.mosl.co.uk/Approved-Codes-of-Practice-Recommendation)

<sup>4</sup> See: [CPM046 and CPW133 Approved Codes of Practice \(mosl.co.uk\)](https://www.mosl.co.uk/CPM046-and-CPW133-Approved-Codes-of-Practice)

process would include Trading Party engagement, possibly through the RWG or other forums, in order to determine whether the benefits of formalising any individual ACoP outweighs the related costs. The FRR notes that the ACoP assessment process will consider the impacts on innovation, while also suggesting that by setting minimum standards only, Trading Parties would continue to be able to provide enhanced levels of service to meet their customers' requirements.

### **Existing enforcement mechanisms should be adopted for ACoP compliance**

The majority of responses were supportive of using the existing mechanisms within the Market Codes for the enforcement of ACoPs, noting this provides consistency with other Code requirements and compliance activities and the development of a separate enforcement structure would add unnecessary cost and complexity. Four respondents advised that they did not support the use of current enforcement mechanisms for ACoPs, suggesting that this would require a significant change in operations to meet the statutory requirements, and the ambiguity of the ACoP approval process needs to be addressed before they can support the proposed enforcement mechanisms. The Proposer stated that the driving principle behind the Proposal is to utilise existing Market Code processes, where possible, instead of developing entirely new processes, recognising the robustness of the current Code Change Process.

### **CCC recommendation**

The Code Change Committee (CCC) considered this Change Proposal at its meeting on 23 August 2022. It voted by majority to recommend that Ofwat approve this Proposal (seven votes in favour of approval and two votes in favour of rejection). The CCC noted that the Proposal would place a formal obligation on Trading Parties to comply with the RWG's good practice guides, addressing the issue of Trading Parties' varying level of adoption. In addition, the CCC acknowledged that codes of practice can be a good reference for Trading Parties and customers, noting that the separate suite of documents within the Codes would support transparency and the availability of information for both Trading Parties and customers.

The two Committee members that voted against the Proposal believed that the proposed framework could add additional complexity, confusion, misunderstanding, contradiction and risked inhibiting innovation.

### **Our decision and reasons for our decision**

We have considered the issue raised in the Change Proposal and the supporting evidence submitted in the Code Change Committee's FRR, including the consultation responses from stakeholders. **We have decided to reject this Change Proposal** as we do not consider that this Change Proposal has sufficiently demonstrated the added value to business customers

through implementation of this Change Proposal that cannot be achieved through the existing market change mechanisms.

Given the lack of any clear and demonstrable benefit from the proposed ACoP framework, along with the ambiguities that we discuss further below, we are of the view that this Change Proposal will not advance the **Primary Principle** of protecting and promoting the interests of, and participation by, existing and future Non-Household Customers. In addition, we have considered our primary and secondary duties under section 2 of WIA91.<sup>5</sup> We do not consider that this Change Proposal protects the interests of existing and future customers, nor do we believe that this change is conducive to the principles of best regulatory practice as we have not seen clear evidence that this Change Proposal would achieve benefits for the market which could not be better achieved through the established mechanisms.

We recognise that this Change Proposal intends to establish a framework for future ACoPs to be introduced within the Codes, and therefore any realised benefits from its implementation would likely only be realised in the medium-long term. While the Change Proposal does facilitate the introduction of ACoPs that are expected to provide consistency and clarity for Retailers and end customers, the proposed framework itself does not fundamentally address the issue of misaligned policies across wholesale regions that would promote customers' interests.

The Proposal as presented does not sufficiently consider or evidence why the formalising of RWG guidance cannot be realised using the existing Code Change process. For example, the Change Proposal sets out that ACoPs would have substantially the same process for implementation as WRC changes. Given that the implementation of ACoPs will have the same processes as a WRC change, the benefit of having both forms of governance in place concurrently is unclear.

We think that the proposed legal drafting could also create further ambiguity. In particular, we think that the drafting of the proposed obligations in the market terms, section 4.23.4), would make it difficult for Ofwat to enforce or for Trading Parties to have certainty on whether they are in compliance due to its subjective nature. We believe that this element of the proposed framework has therefore not been sufficiently developed.

Although supportive of the underlying principle of the Proposal (to improve customer outcomes by reducing unnecessary costs and inefficient interactions between Wholesalers and Retailers across the market), it is unclear how the proposed ACoP framework will drive benefits for end customers. The Proposal's legal drafting does not provide details of the process that would underpin the assessment and subsequent implementation of proposed ACoPs, including how customer outcomes are considered in this process. The proposed legal drafting additionally is unclear as it leaves the establishment of a governance process for

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<sup>5</sup> The duties for most of our work as the economic regulator of the water sector are laid down in sections 2 and 3 of the Water Industry Act 1991 (WIA91) as amended. See: [Water Industry Act 1991 \(legislation.gov.uk\)](https://www.legislation.gov.uk)

ACoPs to a later date and only states in a proposed amendment to the WRC that the implementation of ACoPs will follow “substantially the same process for [WRC] Change Proposals”. Furthermore, the governance process to implement a new ACoP is set out in a proposed amendment to the WRC, whereas governance issues are normally codified in the MAC. Given the ambiguity in the legal drafting and governance processes it is difficult to be confident therefore that the Change Proposal would further the **Transparency and clarity** and **Simple, cost effective and secure** supporting principles.

### **Industry can support the Proposal's intended outcomes**

While we note that the existing Change process allows for the formalising of guidance within the Codes, we are of the view that there is scope for further self-regulation in the market such that good practice guidance is elevated through stronger commitments from Trading Parties. We acknowledge that there may be legitimate reasons for differing policies and processes. However, we are of the view that there is scope for Wholesalers to standardise processes where appropriate, such that the intended outcomes can be achieved without the need for codification. For example, the RWG Wholesale Tariff Simplification Sub-Group collaborated to develop a standardised template for Wholesale Charging statements.<sup>6</sup>

We think that there are alternative ways in which the adoption of RWG guidance could be achieved without formalising within the Codes. We encourage the market to consider ways in which the adoption of RWG guidance could be further incentivised – for example, the RWG might consider providing a form of 'accredited status' to Trading Parties who comply with its guidance. Where formalising of ACoPs within the Codes is required, we think that existing Code Change process and associated enforcement mechanisms can be utilised.

We acknowledge that implementing the ACoP framework would offer the advantage of establishing a formal link between the RWG, its guidance and the Codes, which does not currently exist. Whilst we are rejecting this Change Proposal, we consider that good practice guidance can contribute to improving customer outcomes and addressing market frictions. We would therefore encourage the RWG to adopt a periodic review of its output such that it can identify whether existing guidance should be formalised within the Codes through the established Code Change process. This proactive approach would also support the RWG in identifying gaps and ambiguity within the Codes that are causing customer detriment, which could be addressed through the development of further guidance. Alternatively, as noted previously, guidance can be elevated through a greater commitment from Trading Parties that is supported by RWG accreditation.

### **ACoP assessment and amendment process**

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<sup>6</sup> See: [RWG Wholesale Tariff Simplification Sub-Group Consultation \(mosl.co.uk\)](https://www.mosl.co.uk/rwg-wholesale-tariff-simplification-sub-group-consultation).

Noting our concerns that the process underpinning the assessment of ACoPs has not been sufficiently developed, the Change Proposal also fails to provide sufficient detail of the process for amending or updating formalised ACoPs. We have concerns that in the absence of a defined pre-assessment process for elevating RWG guidance, the proposed framework does not consider whether guidance should be formalised in the WRC (specific obligations for Parties) or through an ACoP within the Codes (more flexible and outcomes-focused obligations). As such, there may be a requirement for future amendments to revise where obligations sit within the Codes. In the absence of a defined process for amending or updating formalised ACoPs, the proposed framework risks adding complexity where obligations need to be amended or updated. In this respect, we have concerns that the Proposal does not further the supporting **Simple, cost effective and secure** or **Efficiency** principles.

### Revisions to the Code Change process

We have concerns that the Change Proposal has not taken account of the forthcoming revised Code Change process. We recognise that this Proposal was raised prior to the commencement of work to revise the Change process, however, we note that the CCC has consulted on its proposed revisions to the Change Proposal process, which proposes to establish criteria for accepting proposals based on whether the problem has been sufficiently evidenced and whether the problem that is seeking to be addressed can be resolved outside of the Codes.<sup>7</sup> Furthermore, the consultation set out that where a problem is accepted into the change process, MOSL will develop a proposed solution to address the raised issue, which may not align with the solution put forward by the proposer. In contrast, the Change Proposal, intends to formalise guidance as ACoPs within the Codes as the solution to an issue, which in practice may conflict with the revised Change process going forward, depending on the outcome of that review.

We also note that the Strategic Panel has identified alignment of Retailer, Wholesaler and Market Operator processes as a key deliverable in their strategic priorities.<sup>8</sup> To achieve this, the Panel will instruct the CCC to prioritise Code changes that support alignment of industry interactions. Where formalising aspects of RWG guidance is seen to be the most appropriate solution to an issue, the Code Change process could prioritise changes where there is sufficient evidence that the alignment of Trading Party processes delivers benefits to current and future non-household customers. Again, this reinforces our view that the intended outcomes of the Change Proposal can be achieved through existing market mechanisms and the proposed ACoP framework does not deliver added value to the market or end customers.

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<sup>7</sup> See: [Developing an effective code change mechanism - Consultation \(mosl.co.uk\)](https://www.mosl.co.uk/developing-an-effective-code-change-mechanism-consultation)

<sup>8</sup> In September 2022, the Strategic Panel published their key areas of work over the next three years: [Strategic Panel Priorities \(mosl.co.uk\)](https://www.mosl.co.uk/strategic-panel-priorities), pages 16-22.



With consideration of these points, we are not satisfied that implementing a new form of Code furthers the **Proportionality** principle.

## **Decision notice**

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

**Dan Mason**  
**Director, Business Retail Market**