

## Minutes of Ad-hoc Panel Meeting 45a

28 July 2020 | 14:30 – 16:30 | Teleconference

Status of the Minutes: **Final**

### MEMBERS PRESENT

Jim Keohane	JK	Chair	Michael Rathbone	MR	Panel Member (Wholesaler)
Michelle Burns	MB	Panel Member (Associated Retailer)	Helyn Mensah	HM	Panel Member (Independent)
Barry Hayward	AC	Panel Member (Associated Retailer)	Elsa Wye	EW	Panel Member (Independent)
Trevor Nelson	TN	Panel Member (Unassociated Retailer)	Pamela Taylor	PT	Panel Member (Independent)
Nicola Smith	NS	Panel Member (Unassociated Retailer)	Mike Keil	MK	Panel Member (Customer Representative)
Claire Yeates	CY	Panel Member (Unassociated Retailer)	Dan Mason	DM	Affiliated Panel Member (Ofwat)
Mark Holloway	MH	Panel Member (Wholesaler)	Adam Richardson	AR	Panel Secretary
Martin Mavin	MM	Panel Member (Wholesaler)			

### OTHER ATTENDEES

Oliver Robins	OR	MOSL (Minute Taker)	Steve Formoy	SF	MOSL (Observer)
Carol Sgambaro	CS	MOSL (Secretariat)	Christopher Wright	CW	Castle Water (Presenter)
Amanda Hinde	AH	MOSL (Observer)	Christina Blackwell	CB	CC Water (Observer)
Huw Comerford	HC	MOSL (Observer)	John Vinson	JV	Independent (Observer)
Tom Daborn	TD	MOSL (Observer)	Georgina Mills	GM	Ofwat (Observer)
Steve Arthur	SA	MOSL (Observer)	Sean Mills	SM	Ofwat (Observer)
Florentina Monea	FM	MOSL (Observer)	Antoine Schmidt	AS	Thames Water (Observer)

### APOLOGIES

Sarah McMath	Affiliated Panel Member (MOSL)
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## 1. Welcome and Introductions

- 1.1 The Chair welcomed the Panel Members and all other attendees to Ad-hoc Panel Meeting 45a. The Panel was informed that AR would present on both changes for discussion in place of CU, who was unwell and not in attendance.

## 2. Introduction to CPW101/CPM031 and CPW100

- 2.1 The Panel considered a high-level introduction to CPW101/CPM031 and CPW100, presented by AR. AR explained that whilst an element of CPW101/CPM031 sought to examine how credit should or should not be maintained in relation to sites being labelled as COVID19 vacant, CPW100 sought to examine the maintenance of credit specifically where the payment of Primary Charges has not been deferred. Although both proposals touched on the issue of credit to a varying degree, the Panel was invited to consider both proposals on their own merit in terms of bettering the existing provisions within the code.
- 2.2 AR explained that it would be for Ofwat to determine the extent to which both CPW101/CPM031 and CPW100 could be implemented based on the recommendations of the Panel. The Panel observed that, if both were layered in implementation, the combined effect could see all Retailers being required to maintain their Credit Support Requirement at the March 2020 level until they have removed or validated all of their COVID19 vacant flags, and have no deferred payments.
- 2.3 Due to both changes impacting COVID19-related credit provisions, the Panel agreed that both changes should be presented and discussed before voting would commence on either.

## 3. Draft Recommendation Report: CPW101/CPM031 – Unwinding Temporary COVID19 Arrangements in the Business Retail Market

- 3.1 The Panel considered the Authority Timetabled Change Proposal '[CPW101/CPM031: Unwinding Temporary COVID19 Arrangements in the Business Retail Market.](#)' This change sought to unwind the temporary measures currently in place to mitigate the impact of COVID19 on the Non-Household Retail market, as introduced in March, April and May of 2020. The proposed solution would:
  - Extend the ability for Retailers to defer primary charges until the end of October 2020 but cap the maximum deferred amount for each Retailer to a cap equal to 40% of primary charges due from March-July 2020;
  - Require that all deferred amounts are repaid by the end of March 2021 (Parties can agree their own repayment profile but with a backstop re-payment profile is provided where no agreement can be reached);
  - Require Retailers to validate all supply points that became vacant during the COVID-19 period (16 March – 31 July) as vacant supply points under the standard definition of vacancy effective from 1 August 2020 or return them to occupied;
  - Extend the suspension of OPS and MPS charges to the end of September and October 2020 respectively; and

- Require Retailers to maintain credit support requirements at March 2020 levels until they have switched off all their temporary vacancy flags following that status ending at the end of July 2020.
- 3.2 AR explained that CPW101/CPM031 was consistent with recommendations set out in Ofwat’s “[minded to decisions document](#)” that summarised their current position in light of the responses provided to their [consultation on next steps](#) to protect the interests of water customers in the business sector.
- 3.3 DM added that Ofwat considered the lessons learnt from the implementation and operation of earlier changes (made under uncertainty and time duress) as integral when preparing to move into a new normal, particularly with regard to customer engagement and anticipating future emergency measures such as regional lockdowns.

#### **Discussion paused for the introduction of CPW100 (Section 4.1)**

#### **Discussion continued following the introduction of CPW100**

- 3.4 The Panel discussed the importance of clarity over the definition of Vacancy in the current context of the Market. One member stated that even with the current guidance in place, there were areas of concerning ambiguity, for example where a property is legally allowed to open but the owner chooses not to due to uncertainty whether social distancing measures can be reasonably applied. It was recommended that the Ofwat should seek to address this issue in its Decision Document for CPW101/CPM031.
- 3.5 The Panel discussed the importance of retrospectively checking the free text field for supply points (SPIDs) that have been labelled as vacant under the standard rules (“BAU vacant”) before August 1<sup>st</sup>, with AR explaining the practical implication of distinguishing between a BAU vacant and a COVID19 temporary vacant. It was noted that Retailers will not need to obtain additional evidence to justify the indicator if they are already in possession of suitable practical evidence, such as records of customer interaction.
- 3.6 JV queried whether any thought had been given to the possibility of Retailers changing their Yearly Volume Estimates (YVEs) to compensate for the removal of the vacancy flag. AR confirmed that it had and that MOSL would continue to carefully monitor the use of YVEs and if necessary, would build on the monitoring already in place.
- 3.7 The Panel considered the rationale for linking the Credit Support Requirement to the use of the temporary vacancy flag. DM explained that there was a direct link between the temporary vacancy flag, consumption, primary charges and, accordingly, credit support. The expectation was that consumption and primary charges would rise over the next two months as vacant sites move back to occupied. As such, there was a concern that, if retailers reduce credit based on COVID19, they may face a steep rise over a short period as COVID19 measures unwind.
- 3.8 Given the additional risk of the vacancy flag being incorrectly applied in some cases, it was fundamentally important to avoid the idea of a “cliff edge” as referenced in the consultation. CW disagreed with this explanation and stated that because this dramatic fall had already occurred in practice, this change would punish Retailers in advance, rather than protect the market. Furthermore, it appeared inconsistent for Ofwat to predict a dramatic rise in the Credit Support Requirement based on when it was underpinning the unwinding of the use of temporary vacancy flags on an early return to normal.

- 3.9 JV sought clarification on the proposed repayment schedule for deferred amounts and asked whether a defaulting Trading Parties could have their contract terminated based on a disputed amount. AR explained that as per the normal process, disputed amounts do not become due until the dispute is resolved and would therefore not form the basis of a default while a dispute was in process.
- 3.10 A Panel member queried the rationale behind the differential treatment of OPS and MPS charges where OPS charges were proposed to be reintroduced at an earlier date. They suggested that because operations were more likely to continue being affected, the suspension of associated charges should be extended for longer than that for market performance (which was primarily related to the interaction of data within the market). GM stated that, as lockdown eases, Trading Parties have more options regarding on-site processes where the health and safety of their operatives must be carefully considered. GM also indicated that Ofwat viewed the services monitored under the OPS regime as being key facilitators in enabling market performance. GM explained that the key point to consider was the pure fact that Ofwat was indeed proposing an extension to the suspension of both (where the original intent had been for the reintroduction of both at the start of August) rather than the respective length of extensions.
- 3.11 The Panel discussed the maximum amount of primary charges that a Retailer would be able to defer following implementation of CPW101/CPM031, with there being some uncertainty as to whether this value was equivalent to 40% or 60% of primary charges invoiced between March and July 2020. AR confirmed that the deferral cap was set at 40% of primary charges invoiced across this entire period, and explained that the legal drafting referenced the inverse, that being the minimum amount that must be paid (60% of primary charges invoiced).
- 3.12 The Panel observed that the legal text should be carefully reviewed to ensure that it delivered the intent of the change proposal regarding the application of the cap on deferred amounts. The Panel requested that MOSL should review this aspect of the legal text and revert to Ofwat.
- ACTION: A45a\_01**
- 3.13 A Panel Member asked what was envisaged in terms of planning for the development and implementation of incentives with respect to the treatment of YVEs and Vacancy, noting the lack of proposed legal drafting on this point. AR explained that Ofwat was currently considering the appropriateness of a new MPS standard (and associated charge) for vacancy, and SA added that Ofwat were similarly looking at the possibility of adding Additional Performance Indicators around YVEs. SA also referenced the Vacancy Panel Update (17 July) where MOSL took an action to build on the existing framework in place to track changes in YVEs and the use of the Vacant Flag, whilst simultaneously examining the possibility of another audit.
- 3.14 A Panel Member expressed their concern that the audit on vacant sites was not statistically robust.
- 3.15 A Panel member stated that the purpose of maintaining credit support based on the March 2020 P1 was to provide assurance to Wholesalers while their risk of exposure was increased through the combined effect of Retailers deferring charges and using the temporary vacancy flag. Therefore, where a Retailer does not defer, the only additional risk posed to the

Wholesaler is the extent to which the vacancy flag has been applied in error and is underestimating consumption. They proposed that where there is some evidence to suggest significant consumption at vacant properties (which will be charged at some point in the future), there is an argument that the use of the vacancy flag does create a false position. However, the Panel Member stated that they were struggling to get an overall feel for whether a non-deferring Retailer should be treated identically to a deferring one in terms of their Credit Support Requirement.

- 3.16 The Panel discussed the extent to which the measures introduced by CPW101/CPM031 would prepare the market for a second wave, on either a national or regional level. DM explained that all proposals had been underpinned by evidence provided by Trading Parties in the Ofwat consultation and reiterated that the recent implementation of emergency temporary measures, and ensuing experiences throughout the market, should leave parties better prepared for future lockdown scenarios.
- 3.17 A Panel Member asked for clarification on the extent to which the planned resumption of OPS and MPS charges had considered any regional variation in the planned rollout of meter readers. DM stated that whilst anecdotal evidence suggested regional variation in terms of meter reading activity across the market, the development of an all-encompassing solution to account for this variation was difficult. Fundamentally, it would be important for contracting Retailers and Wholesalers to work through future developments (such as regional lockdowns) together using their experience of the past few months. GM added that Ofwat was also cognisant of the dynamic link between switching on performance charges and affecting parties' behaviours and prioritisations. Furthermore, the possibility of a phased reintroduction for example, would add complexity and reduce clarity. The Panel Member suggested that MPS charges do not necessarily incentivise the right behaviours in all situations but noted this was a separate issue to that being discussed.
- 3.18 In response to an earlier comment by CW regarding Section 3 of CSD 0104 'Maintain SPID Data', GM explained that the Ofwat Decision Document would reiterate the need for Retailers to be clear on the legislative provisions they were relying on in their application of the vacancy flag for sites which were prohibited by law from being occupied.
- 3.19 A Panel Member stated that it would be helpful to gain some early understanding around the idea of a small percentage of supply points being exempt from the possible incentive measures, with regard to the removal of vacant flags, to be brought forward in October. GM explained that had not yet been thought out in detail, but Ofwat were aware that there might need to be some provision for a small number of exceptions in situations where it proves difficult to get in touch with a customer.
- 3.20 A Panel member stated that it was important for the Panel to have early sight of the development of criteria and incentives with regards to the vacancy and YVE situation, and reiterated the importance of being able to take confidence from meaningful and statistically significant monitoring and sample data. SA agreed, and noted that MOSL would be pursuing this.
- 3.21 CW questioned whether the proposed drafting for Section 9.12.3 (d) of the Business Terms delivered the intent of CPW101/CPM031, because it appeared strange that a Retailer would need to wait until October 2020 to benefit from the removal of all temporary vacancy flags even if this was completed in August. GM confirmed that this was the intended effect of the

drafting and explained that this provision had been constrained by responses from Retailers to the Ofwat consultation which had implied that an orderly unwinding of temporary vacancy flags would take time. Essentially it had been deemed very unlikely for any Retailer to have achieved this before the October 2020 P1 run was carried out in September. CW indicated that, in his view, the restriction set out in this clause would undermine the incentive.

- 3.22 A Panel member queried whether Ofwat had given any thought to the likelihood of consumption not fully returning to pre-COVID19 levels, and therefore the pre-COVID19 levels of Credit Support being unsuitable as a reference point for the future. DM confirmed that Ofwat had recognised the potential for this, hence the different options presented within its consultation. Fundamentally, the consultation responses had not presented a compelling case for differential treatment in terms of deferred payment but had strong support for linking credit support and temporary vacancy.
- 3.23 Before voting on CPW100/CPM31, the Panel considered and discussed CPW100 (Section 4.1 to Section 4.7 below).
- 3.24 The Panel:
- **AGREED** (unanimous) to recommend the implementation of CPW101/CPM031 to Ofwat for approval;
  - **AGREED** (unanimous) to recommend an implementation date of 1 August 2020, if Ofwat approval is received by 30 July 2020.
- 3.25 Several Panel members explained that their votes had been made on the condition that the Panel receives early insight of any incentives related to vacancy and YVEs and how the criteria for these will be decided and subsequently reported.

## 4. Draft Recommendation Report: CPW100 – Revisions to Credit Support Requirements under CPW095

- 4.1 The Panel considered Change Proposal [‘CPW100: Revision to Credit Support Requirements under CPW095’](#). This change sought to remove the requirement for a Retailer to maintain its Credit Support Amount at the same level as set out in the Credit Support Notices issued following publication of March 2020 P1 Settlement if the said Retailer had chosen not to participate in [‘CPW096: Payment Deferral \(Medium Term\)’](#).
- 4.2 Panel Members noted that CPW100 had previously been raised as an Urgent Change Proposal and discussed on 15 June 2020, with the Panel then concluding that it did not meet the Urgent Change Proposal Criteria and requesting for further evidence (subsequently provided through Ofwat’s [consultation on next steps to protect the interests of water customers in the business sector](#)).
- 4.3 AR explained that should the Panel wish to focus on any confidential information that had been provided to Panel Members through this consultation, then the meeting would need to go into closed session, however the high level findings should be sufficient to facilitate open discussion and voting.
- 4.4 The Panel noted that the majority of respondents had expressed a preference for credit support requirements to be maintained at March 2020 levels until all the temporary vacancy

flags are switched off, rather than allowing credit support requirements to be calculated on the basis of primary charges owed in any given month.

- 4.5 The proposer of CPW100, CW, thanked the Panel for their forbearance and provided some further justification for the Change Proposal. CW stated that the apparent shift in rationale for maintaining the Credit Support Requirement at the March 2020 level, namely to provide incentive for Retailers to remove their temporary vacancy flags at a faster rate, was untenable given the cost to Retailers of calculating credit support based on incorrect consumption, and given the original incentive of the temporary vacancy flag to protect customers from excessive and unjustified bills unrelated to their consumption. CW also highlighted the lack of reference to customer impact in the responses to the Ofwat consultation. CW noted that it is entirely in the Retailers interest to establish consumption and charge accordingly (provided the charges are correct), and it should be considered that maintaining the disconnect between consumption and credit support runs counter to the principle of efficiency and the interest of customers.
- 4.6 CW explained that Castle Water had replaced approximately 9000 temporary vacancy flags to occupied status in the past week, and one in five subsequent bills had been the subject of customers getting in touch to complain. On this subject, CW suggested that Ofwat and CC Water should campaign to encourage customer reads. The assumption that customers are operating normally, and to base Credit Support Requirements on this, is inconsistent with reality and the expected return to BAU.
- 4.7 CW concluded by stating that should the Panel choose not to recommend CPW100 to Ofwat, and decide that credit support should be maintained at the March 2020 level, then there would need to be a full impact assessment in terms of compliance with the Objectives and Principles.

### **Discussion paused for the consideration of CPW101/CPM031 (Section 3.3)**

#### **Discussion continued following the conclusion of voting on CPW101/CPM031**

- 4.8 Several Panel Member expressed their inclination to support CPW100, noting the benefits against the Objectives and Principles that had been outlined by the proposer. They agreed that deferred primary charges increased the indebtedness of Retailers and the potential impact associated with Retailer payment default. This, in turn exposed customers to a higher degree of risk.
- 4.9 A Panel Member queried the degree of customer benefit provided by CPW100 given that the effect of its implementation, that being non-deferring Retailers having the opportunity to pay a lower level of credit support, might only be in place for approximately two months if this was superseded by the implementation of CPW101. CW explained that for Castle Water, this effect was material as it would free up £60,000 that could be spent on customer service at a time of exceptionally high demand. Furthermore, excessively high credit support reduces a Retailers' ability to pay Wholesale charges.
- 4.10 The Panel discussed the interaction between CPW100 and CPW101/CPM031. Panel Members enquired what might happen if both CPW100 and CPW101 were recommended by the Panel for approval. AR explained it was not clear how Ofwat might treat each Change Proposal, whether Ofwat might approve one or the other or, potentially, vary its approach to implement

a combined solution. As such, it was important for the Panel to consider CPW100 as a separate change, on its own merits, against the current code baseline. However, should Ofwat contemplate an overall change that incorporated CPW100 and CPW101/CPM031, it could be that a Retailer would need to remove all temporary vacancy flags and have no deferred payments in order to benefit from a normal Credit Support Requirement (from the start of August 2020 until the end of March 2021). It was subsequently suggested that the implementation of CPW100 alongside CPW101/CPM031 would create a “double lock” against the normal application of credit support.

- 4.11 AR stated that the Panel should consider both changes against the baseline before discussing any interaction effect; deliberations and recommendation on the latter could be captured in the minutes and the ‘Panel Recommendation’ Section of the two Final Recommendation Reports.
- 4.12 A Panel Member stated that extra complexity introduced by CPW100 was not justifiable by the extent, or duration of its benefit, and was unnecessary given what was presented in CPW101/CPM031, which they supported. Another Panel Member agreed and suggested that the combined effect of CPW100 with CPW101/CPM031 could result in more Retailers being locked at a higher level of credit support. In contrast, another Panel Member stated that both changes sent a strong indication of the intention to support a robust market that protects end customers by maintaining suitable collateral amounts at high levels of risk, especially where we are unsighted on the true extent of vacancy.
- 4.13 CW explained that the “double lock” effect was an unintended consequence of the change proposal being considered at the same time as CPW101/CPM031 and questioned the practice of considering two changes in unison. CW suggested that there was a risk of the Panel being prejudiced against CPW100 by assuming the implementation of CPW101 and expressed concern that further discussion had ensued after several members had already expressed their intended vote. This view was shared by several Panel Members.
- 4.14 A Panel Member explained that were leaning toward abstaining from the vote. They suggested that the interaction effect could cause additional problems for customers and expressed concern at the lack of clarity under which the Panel was voting. Another Panel Member stated that the provision of collateral was a method of protecting customers. They stated that CPW101/CPM031 addressed the risk from the perspective of temporary vacant flags and whether their application reflected true COVID19 vacancy, whilst CPW100 considered the additional risk posed by a Retailer who defers payment. In either case, there is level of exposure, and therefore any decision not to support either change proposal would be inconsistent with the purpose of collateral.
- 4.15 Another Panel Member stated that they were supportive of CPW100 in isolation, but shared concerns over the additional complexity being introduced, and whether it would deliver the proposer’s intent due to the interaction with CPW101/CPM031. AR reiterated that the change should be considered in isolation and any concerns over the interaction effects would be captured qualitatively. The Panel Member noted how the consultation feedback indicated that neither Wholesalers and Retailers expected consumption to return to ‘pre-COVID’ levels by the end of the year, and as such, it appeared inappropriate to require credit be lodged at ‘pre-COVID’ levels.

- 4.16 Several Panel Members disagreed over the extent of the interaction effect, with one member stating that it presented a double test to be passed for all Retailer to achieve a normal level of credit support, with another member suggesting that not all Retailers would be impacted. They stated that a vote against either proposal would not suit the interest of customers and suggested that any associated problems could be effectively mitigated so long as the temporary changes were unwound as encouraged by Ofwat. Another member stated that the interaction effect needed to be better communicated to Panel.
- 4.17 The Panel:
- **AGREED** to recommend the implementation of CPW100 to the Ofwat for rejection (5 in favour, 3 against, 4 abstained)
  - **AGREED** to recommend an implementation date of 1 August 2020 should Ofwat approve the change and approval is received by 30 July 2020.
- 4.18 The Panel Members who abstained felt that maintaining credit support requirements at the March P1 level overstated the credit risk of Retailers, particularly in relation to anticipated levels of consumption. Several also expressed concerns that the desired outcome of the Proposer would not be delivered, if Ofwat combined CPW100 and CPW101/CPM031 so that a Retailer would be subjected to a higher threshold of having to pay off all its deferred charges and remove the temporary vacancy flags before it could revert its credit support requirements to a normal level.
- 4.19 The Panel Members who voted against CPW100 expressed similar concerns about how the change sat alongside CPW101. It was suggested that the implementation of an overall change that incorporated the two separate principles of linking credit support to deferred charges, and linking credit support to temporary vacancy, would introduce significant additional complexity that would in turn inhibit the unwinding of credit support requirements. On balance, these members felt that they could not support CPW100 based on their support for CPW101.
- 4.20 The Chair summarised the key qualitative learnings to be taken from the discussion on CPW100 and CPW101/CPM031. These consisted:
- a recommendation for the guidance regarding vacancy to be revisited in recognition of its importance going forward to a “new normal”;
  - a request for careful monitoring and reporting from MOSL in the changing status of vacancy and application of YVEs (including consideration of statistical significance);
  - a recognition that the target date for removing the vacancy flag requires careful consideration to ensure that the unwinding process is coordinated with due diligence;
  - a request for Ofwat to carefully consider whether in principle, it is more appropriate to link credit support requirements to temporary vacant supply points or to deferred primary charges;
  - some concerns over the application of MPS and OPS charges and the timing of their reintroduction; and



- the importance for the Panel to learn from the experience of considering interacting proposals. Several Panel Members stressed the importance for deliberations to be completed in full before a vote is conducted.

4.21 CW requested for his reservation over the voting process for CPW100 be captured in the minutes and Final Recommendation Report for CPW100. CW stated that the voting process had been stop-start in nature, and had allowed for some Panel Members to change their votes from support to abstain based on subsequent discussion on the interaction with CPW101/CPM031, rather than relying on the baseline market conditions for comparison.

## 5. AOB

5.1 There was no other AOB and the Chair closed the meeting.

## 6. Actions

Action Number	Action
<a href="#">A45_01</a>	MOSL to ensure that the legal text for CPW101/CPM031 delivers the intent of the change proposal regarding the application of the cap on deferred amounts.

## 7. Post Meeting Addendum

Following concerns expressed at the Panel Meeting regarding the deliberations and voting on CPW100, and after discussions with the relevant Ofwat representatives who had also expressed their concerns regarding deliberations on CPW100 (and stated that it may be appropriate to re-convene the meeting), the Chair felt that it was appropriated and determined to re-convene the Panel as soon as possible to ensure that the Panel’s decision-making was clear and that there was no confusion on the effects of a proposed change or the basis on which a Panel recommendation was made.

Ad-hoc Panel meeting 45b was convened on 30 July to enable Panel Members to ask any further clarificatory questions on CPW100 before taking a final vote on the recommendation to Ofwat regarding this change. At this meeting, Panel Members agreed that the recommendation and vote of the Panel regarding CPW100 at Panel Meeting 45a would be disregarded.

The deliberations regarding CPW100 at meeting 45b are set out in the minutes of that meeting.