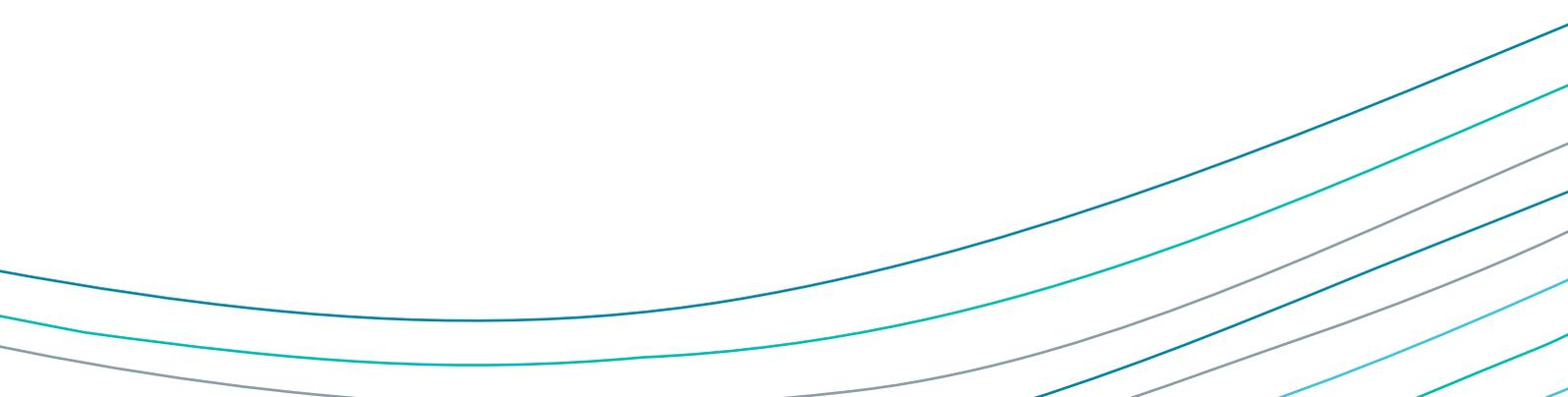


Quarterly Market Review
Q1 2018/19



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Foreword



Welcome to our Quarterly Market Review. It is in a new format, focused on the most significant market issues and developments.

We report here on a wide range of initiatives to tackle and resolve market issues, we share our take on key

market trends, and we report on how MOSL is performing against our objectives. With the market now firmly into its second year, more operational updates such as switching and market share analysis will be covered in our monthly Market Focus.

As we all expected there has been no let-up in the pace of work in this the market's second year, and indeed an increase in the range of initiatives underway to tackle challenges and take opportunities.

The palpable energy across this developing market is reflected in this report. The new information and updates cover a wide range of areas including: our assessment of latest market trends; the market audit; digital and technology initiatives; progress on our plans to relocate to Southampton; progress against our key performance indicators; and the MAC Panel proposal to Ofwat for a delay in running RF Final Settlement reports. You will see here a number of new initiatives to improve market efficiency reflecting this priority for us: the new Market Improvement Strategy; the Panel Plan; the Market Issues Register; and the Market Performance Operating Plan.

Our first Annual Market Review, and indeed Ofwat's State of the Market Report, showed that while the market had come a long way in just one year, there were important challenges to tackle such as the quality of data. MOSL's Strategy Statement shows that the Board has put addressing these challenges as a priority centre stage.

We have started to make Market Performance Standards (MPS) results public for the first time and introduced MPS charges as planned – these are important tools to help push performance up. The Market Improvement Strategy will shine a light on performance issues at the root of market friction, escalating them when they are not quickly resolved. The Market Performance Operating Plan outlines the priority issues with the greatest impact on the market and our plans for resolving them.

Market governance is an area of great interest to members and we have been working to improve our voting arrangements and Board composition to allow better engagement, and ensure all three categories of membership have an opportunity to be heard. Members voted in favour of the Board's recommendation to give associated retailers the same voting rights as wholesalers and unassociated retailers, and to create a new non-executive Board director position, filled through an election by the associated retailers. Also, the post of Board director elected by unassociated retailers – currently held by John Reynolds – is coming up for re-election. Both elections are taking place on 3 September 2018.

Engagement with our members is key to our success. I am aware that some would have welcomed more engagement around the decision to relocate out of London, and I am keen to ensure that we engage more fully in future.

I am looking forward to working closely with all stakeholders as we deliver the MOSL strategy and Business Plan objectives, during what promises to be an exciting time for this market. I recently launched this year's CEO Survey which is an important channel for member CEOs to provide input to MOSL Board as we develop the 2019/20 Business Plan, and I would encourage you to make your views known by the closing date of 7 September.



Chris Scoggins

Chief Executive Officer,
Market Operator Services Limited (MOSL)

“ I am looking forward to working closely with all stakeholders as we deliver the MOSL strategy and Business Plan objectives, during what promises to be an exciting time for this market ”

Market trends

- ◆ Since April 2018, five new retailers entered the market: Coca-Cola European Partners, Blackpool Borough Council, Smarta Water, Utility Bidder and Tor Water
- ◆ Castle Water acquired Water Choice during the quarter with c.50,000 supply points transferring to Castle Water in June 2018
- ◆ The total number of supply point switches, to the end of July, stood at 156,150. This represents 5.8% of the 2.7 million supply points in the market and 12.6% at a consumption level
- ◆ July saw the fourth highest switching rate since the market opened and the second highest in 2018 with new entrant retailers achieving the largest gains, in part, supported by the increased use of brokers. This follows June's particularly low level of switching
- ◆ We have seen a substantial improvement in Wholesaler performance against the Market Performance Standards (MPS) with overall achievement in June surpassing 75%, compared to 64% at the end of the previous quarter. Whilst this marks a significant improvement, there continues to be a large range in the level of performance of wholesalers on new connections and meter reading. We will continue to monitor this over the coming quarter
- ◆ Retailers have continued to perform consistently in MPS terms at a market level across the last six months with an average achievement rate of 75% across five of the six months. There was a dip in performance in May 2018 as meter reads due for biannual meters were not submitted for the second time since market opening. This market issue can have a significant impact on the efficiency of settlement and we will seek to address this as a priority through our Market Performance Operating Plan activity

“ The total number of supply point switches, to the end of July, stood at 156,150. This represents 5.8% of the 2.7 million supply points in the market and 12.6% at a consumption level ”

◆ We did however, see large numbers of historic meter reads submitted by retailers at the beginning of the quarter (known as “data cleansing”). Whilst this was in many ways positive, as it increased market consumption information, it did affect the MPS performance of retailers. June saw the first month this year without a material number of these very late, data cleanse, meter reads submitted and enabled a better view of how the market is performing on more of a ‘business-as-usual’ basis. We were pleased to see that in June, a majority of retailers had an achievement of over 90% on the cyclic meter read submission standard. This is one of the highest volume tasks that retailers undertake and plays a vital role in ensuring accurate settlement

◆ This quarter also saw a large number of monthly meters reclassified to their appropriate biannual read-frequency as a further demonstration of data cleansing activity where their read frequency had been incorrectly set. This was a joint effort between wholesalers, retailers and MOSL and provided a good example of co-working between market participants. These re-classifications enable retailers to focus on ensuring all large consumption supply points are read monthly and that meter reading MPS performance is accurately reflective for a retailer’s portfolio

The market in numbers

Data for Quarter: April - June 2018



Market improvement update

Our User Forums have continued to provide a key engagement opportunity covering a variety of market issues, with a prevailing theme of moving towards a more planned approach to market improvement. There has been a focus on introducing the Market Improvement Strategy and Market Performance Operating Plan.

Feedback on these items has reflected that there is strong support for a prioritised and co-ordinated approach to market issues with a recognition that this approach will necessarily mean some areas will need to be addressed at a later date.

We introduced Market Performance Charges and published the first set of Market Performance Standards charts and data in May. This followed close working with the MPC on the revised set of MPS and the new MOSL reporting capability for those standards.

Market Improvement Strategy & Market Performance Operating Plan (MPOP)

There has already been a good deal of work to improve the market by many parties, but it's time to move to a more planned approach that pulls work together in an agreed and prioritised way that enables focus on the most important areas and facilitates tracking of progress. We therefore launched our Market Improvement Strategy in June.

The strategic goals for this improvement work are:

- ◆ Reducing friction in the market, enabling the market to operate efficiently
- ◆ Promoting effective competition

The issues relating to these goals have been developed through engaging with trading parties, Defra, Ofwat and others and the development of a Market Issues Register.

Building on this, our Market Improvement Strategy provides the framework for a staged approach to driving improvement based on market outcomes.

The Market Performance Operating Plan (MPOP) builds on this framework and shows the planned approach to these outcomes, issues, improvement steps and timescales for the next 18 months.

Sitting within the strategic goals, the high priority outcomes targeted through our MPOP are:

- ◆ Enabling efficient settlement
- ◆ Enabling efficient switching
- ◆ Level playing field for retailers
- ◆ Improving trading party experiences

Improvements to settlement efficiency will address the challenges being seen in the early market in ensuring that actual consumption information is used as the basis for settlement wherever possible and, where this is not the case, that robust estimated consumption information is provided by trading parties. This work will include the enabling work required to improve the means by which meters can be located, accessed and read in a timely manner and how the vital data sets relating to estimated consumption can be addressed.

An efficient switching process is key to non-household customer experiences in the market. We have seen issues affecting this process relating to the pairing of a customers' water and wastewater services in addition to issues relating to the timeliness and basis of the meter read taken as part of the switching process. These will both be addressed as a high priority in the MPOP work.

We will also continue the work on improving the processes and ways of working related to trade effluent arrangements which have been seen to cause challenges in the early market. The MPOP also addresses issues related to the arrangements by which trading parties interact with each other through multiple bilateral arrangements. Both the trade effluent and bilateral work are seen as contributing to an outcome focused on improving trading party experiences in the market.

Other existing workstreams within the MPOP framework include the introduction of charges for wholesalers against the Operational Performance Standards (OPS), these standards set out the performance levels expected of wholesalers in delivering services to retailers.

Regular updates will be provided to trading parties, via the User Forum, and to market governance groups on progress against the prioritised outcomes covered in the MPOP and we look forward to seeing the benefits being realised for both trading parties and end customers.

Market audit

The year one audit of the market was carried out by PwC. It provides trading parties and MOSL with an independent review of both trading party and MOSL compliance. Key areas of note for trading parties and MOSL were:

- ◆ Pervasive market data quality issues, particularly noted with meter master data, management of shared SPIDs and eligibility criteria
- ◆ Widespread challenges in interpretation and deployment of code into operational processes, for example disconnections and sensitive customers
- ◆ Inefficiencies and complexity in bilateral processes, such as new connections, leading to challenges in adhering to SLAs and meeting customer expectations
- ◆ Completeness and accuracy of meter reads, caused by insufficient validation procedures, and quality and timely cyclic and transfer reads
- ◆ Issues in CMOS functionality impacting data quality of vacancies, tariffs and bulk supply, and effectiveness of processes leading to increased costs of service
- ◆ Complexity and inconsistency in operation of Trade Effluent processes resulting in issues in applications of consent, challenges in catering for one-off discharges and an adverse impact on the customer

We have reviewed the key themes identified by the audit at a granular level and provided a management response to each of the findings. The issues have been analysed and reviewed and fed into the market issues assessment process and the development of the MPOP, which prioritises the work we will undertake with the industry to resolve market issues. Trading parties have also provided management responses to their specific audit findings for which progress will be reviewed in the Year two audit.

Following the audit, PwC have issued an ISAE300 Reasonable Assurance report which provides reasonable assurance that Settlement is operating in line with the calculations set out in the Codes as at 31 March 2018. This report has been issued to trading parties and is available to be used to provide an input to their revenue assurance process.

MOSL is currently working with PwC to define the scope for the second year audit. The goal will be to use data in a more sophisticated way, to identify non compliance and identify challenging behaviors from trading parties. The market audit will complement the other market improvement initiatives undertaken by the Panel, MPC and other industry groups.

Market Design

Market Change

Since April we have supported the Panel in considering 11 Change Proposals.

Change	Title	Panel determination	Status
CPM002 (MAC005)	Data Protection Updates	Approved the withdrawal of this change	Withdrawn
CPM008	Redistribution of Market Performance Standards Charges	Delegated responsibility to the Market Performance Committee to consider CPM008 following a request from Ofwat for further assessment	Currently under assessment
CPM011	MOSL Invoices and Payment Terms	Recommended that Ofwat approve the change	Implemented on 31 July 2018
CPW010	Emergency Contact Details	Recommended that Ofwat approve the change	Awaiting Ofwat decision
CPW019	Alternative Eligible Credit	Recommended that Ofwat approve the change	Implemented on 31 July 2018
CPW034	Housekeeping changes to CSD 0301	Recommended that Ofwat approve the change	Implemented on 25 May 2018
CPW035	F01 Form Amendments	Recommended that Ofwat approve the change	Awaiting Ofwat decision
CPW036	G/02 Form Amendments and G/03 Temporary Consent Form	Recommended that Ofwat approve the change	Approved by Ofwat for implementation on 28 September
CPW037	Removing the Error Codes list from CSD 0301	Recommended that Ofwat approve the change	Awaiting Ofwat decision
CPW038	Tariffs Report updates	Recommended that Ofwat approve the change	Awaiting Ofwat decision
CPW039	Deferral of Final Settlement Runs	Recommended that Ofwat approve the change	Awaiting Ofwat decision

Review of Credit Provisions

In late 2017, Ofwat commissioned a review of the credit arrangements in the non-household water retail market. Ofwat published the results of the review on 15 June 2018. It made recommendations in a number of areas and highlighted the following matters for Panel consideration:

- ◆ Ensuring greater transparency of PCGs and alternative credit arrangements
- ◆ Reflecting payment history in order to access an unsecured credit allowance
- ◆ Clarifications around credit assessment scores
- ◆ Reviewing termination, default and interim supply processes
- ◆ Consideration of pooled credit models

The Panel has sought nominations from trading parties for a Credit Committee to consider these matters.

Final Settlement Runs

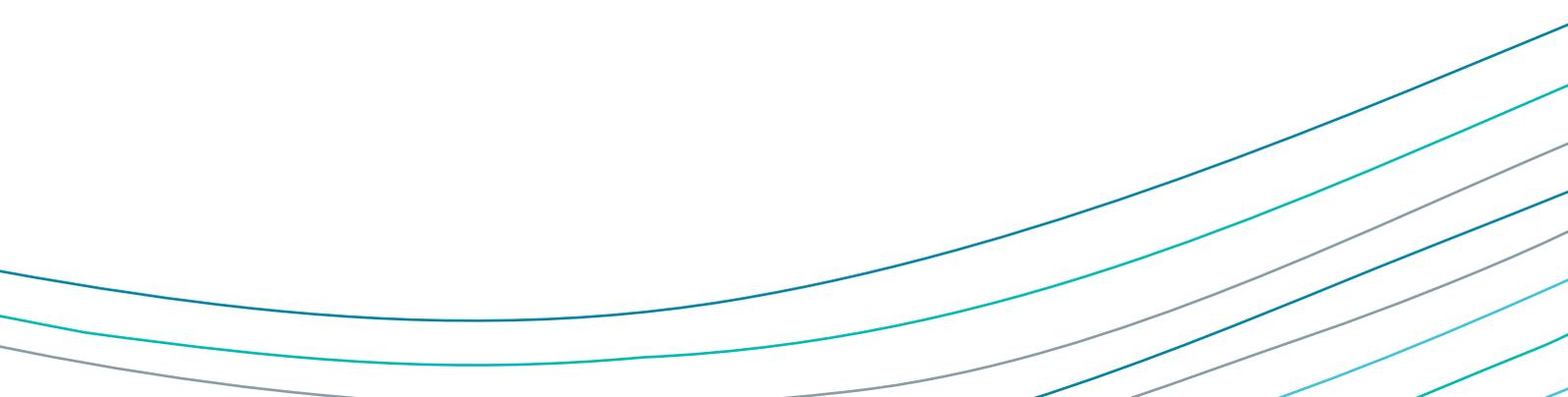
In June the Panel discussed the Final Settlement Run for April 2017 - the first month of live operation for the non-household water retail market - which is due to take place in September. These calculations represent an important milestone in the new market, as they lock in consumption data associated with Supply Points and crystallise the charges calculated for each customer premise. Some Panel Members expressed concern that some meters were still settling on estimated, rather than actual, reads.

There were different views on the Panel on how best to address the data quality issues, to strengthen the market and give customers certainty through accurate bills.

Having considered feedback from 20 trading parties and MOSL, the Panel recommended to Ofwat a deferral of Final Settlement Runs (Change Proposal CPW039). The proposed deferral was for no more than 12 months.

Panel Members felt a deferral of final settlement runs would provide further time for trading parties to carry out data correction projects to rectify incorrect data or submit meter reads. This would enable retailers to generate more accurate bills for the end customer, which the Panel felt would improve the consumer experience. The Panel felt that the time-limited nature of the deferral would provide an impetus for the work needed by trading parties to improve data quality.

Ofwat will decide whether to approve or reject the Panel's recommendation for a delay.



Panel Plan

We are supporting the Panel in putting in place its first Panel Plan. The Plan sets out three priority areas:

Promoting effective competition

- ◆ Consideration of the credit provisions set out in the market codes
- ◆ Review of new connections processes to ensure they are fit for purpose before coming into effect in the market codes in April 2020

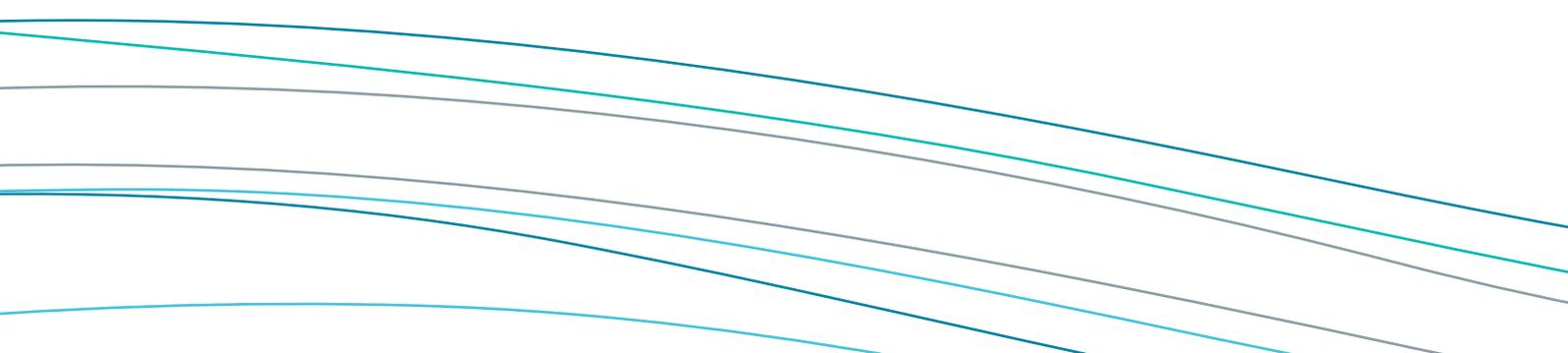
Reducing friction in the market, to enable the market to operate efficiently

- ◆ Evolution of the Market Performance Framework to deal with areas where the market may be underperforming, and where concerns about the accuracy of settlement could constrain effective competition or create friction within the market
- ◆ Review of the Trading Disputes and Trade Effluent provisions to make sure they are efficient and effective
- ◆ Consideration of bilateral arrangements with particular focus on the complexity of wholesaler /retailer interfaces

Embedding good working practice and efficiency in market code governance

- ◆ Review of change proposal and document architecture provisions to ensure best practice and efficient and effective progression of change
- ◆ Review of Panel committees to ensure they are proportionate and that all trading parties' views (large and small, new entrant and incumbents) feed into decision-making
- ◆ Post-implementation review of the code provisions that support the General Data Protection Regulation (GDPR)

The Panel Plan was published in July. We have invited trading parties to feedback on the priority focus areas.



Digital and technology initiatives

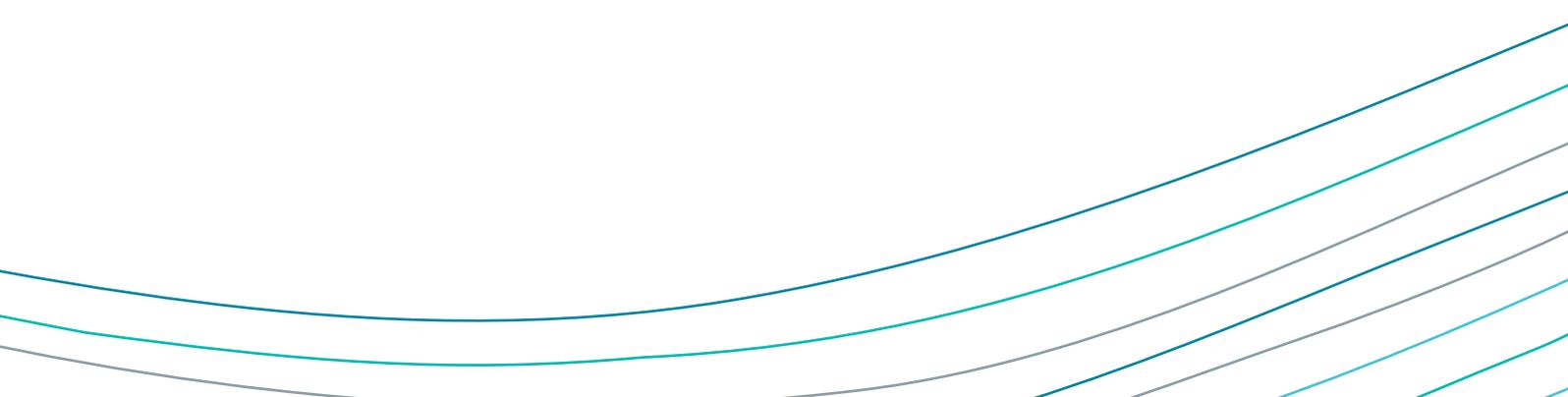
We have worked to improve the CMOS experience for trading parties. We now have a Medium Volume Interface (MVI) capability which complements the existing batch interface and portal access available for users. Trading parties are able now to transact in bulk, without having to invest in complex IT infrastructure.

Our Market Performance Framework (MPF) reporting suite was also deployed, and this supported the commencement of performance charging on 1 April, to make the process simpler and more intuitive.

CMOS Release 4.0 was deployed into Production environment on 19 May on schedule. This Release delivered two Code changes: SPID New Connection Allocation and improvements in the reporting of meter read rejections – as well as resolving 89 outstanding service defects.

The Digital Strategy Committee has been working with industry to consider and suggest solutions for the issues that bilateral engagement between trading parties can present. This work has been instrumental in providing us a better view of the issues, along with ways to improve and resolve them. Over the next quarter, the group will engage with industry groups to find a consensus view on the best way to progress resolving this significant industry challenge.

On 27 July we delivered CMOS Release 4.5 into Production, which extended capability to manage Final Settlement Estimated Reads. This Release will enable MOSL to work with trading parties to remove all existing Shadow “G Reads”.



Relocation update

In line with the commitments in our Business Plan to reduce costs and to review our office location, the Board has determined that we should relocate out of the London area to Southampton in this financial year. We have progressed quickly with our relocation plan and are on track to complete the move by end of January 2019.

The 2017 CEO Member Survey indicated that trading parties would favour a move, and the vote to approve the cost to enable the relocation last May showed this to be so. The increase of £2.2 million in our 2018/19 budget will enable us to deliver savings of £7.4 million (undiscounted) over a 10-year period and accelerate our move to a stable organisation, in a permanent home that can focus on operating the market in an effective and efficient way.

I will continue to reach out to members who expressed concerns around the re-location to discuss how we can continue to support you and your organisation and maintain a high level of engagement across the industry.

Our transition plan sets out our approach to knowledge transfer, recruitment and engagement.

Office location

We have identified two potential office locations in Southampton, both providing a good future home for our staff, and a hub for trading parties to meet. Our project plans are on track and work is moving forward well. Our current office in London will be vacated by January.

Engagement

We are working to ensure that the new office fitout incorporates the appropriate technology to facilitate remote access to member meetings and forums, and will look to update on this by the next quarterly review.

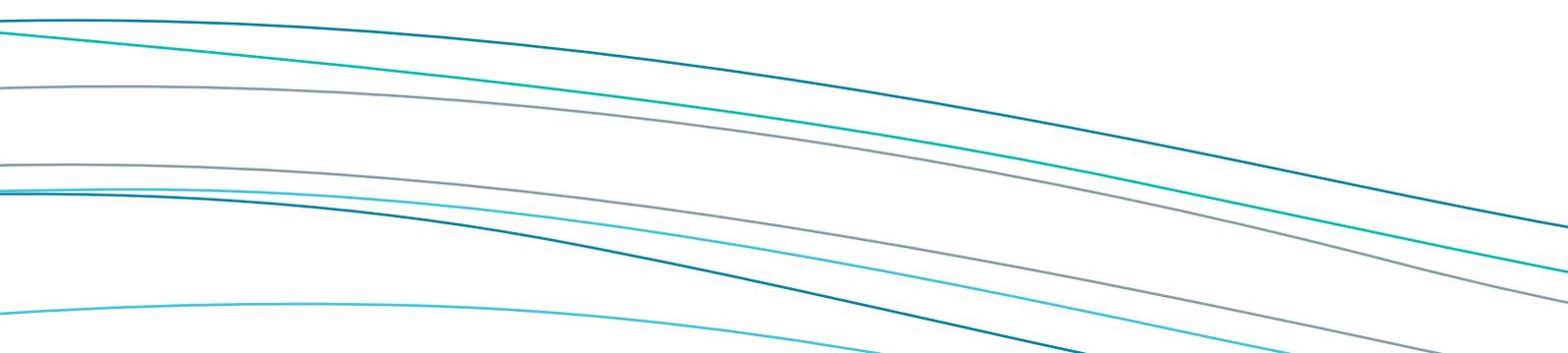
Recruitment

Making sure we attract, hire and retain high quality talent is central to our plans. A recruitment firm has been engaged to help bring in new colleagues during the transition. Improvements are being made to the recruitment and candidate sections of the MOSL website to make sure we fully convey the attractions of working for MOSL. Short term hires are being made where appropriate to help us deliver our 18/19 obligations whilst relocating, and we have made sure our recruitment policy reflects our company values.

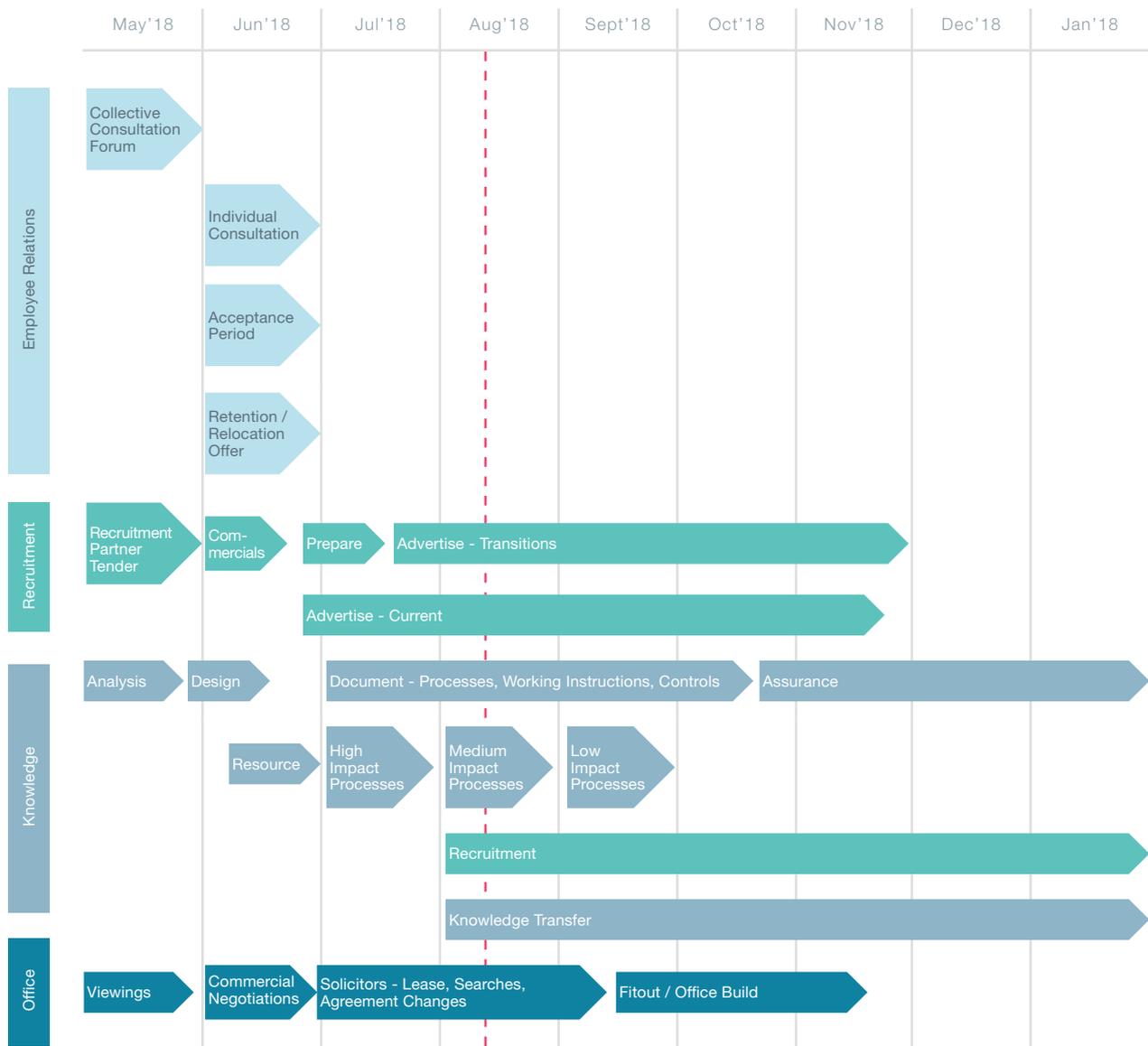
We are making sure we have the resource we need to continue delivering our stretching objectives despite the inevitable disruption caused by a significant relocation.

Knowledge transfer

All MOSL colleagues have completed a comprehensive review of current business processes, and will continue to improve and refine all documentation that will support a robust knowledge transfer. We will also take the opportunity to improve and refine processes where necessary as part of this process.



Transition Plan to January 2019



MOSL service

MOSL KPI	Description	Target	Cummulative position (18/19)	Performance June	Performance May
MO Compliance %/#/high/med/low	For information: MO compliance % is a measure of MOSL compliance with its code obligations categorised by impact to the market (high, medium or low)	100% High impact 90% Medium impact 80% Low impact	98% High impact 99% Medium impact 85% Low impact	98% High impact 99% Medium impact 88% Low impact	98% High impact 99% Medium impact 85% Low impact
Query turnaround time within SLA (6 types of query)	MOSL dealing with queries within SLA	85%	88.50%	90%	90%
Settlement timeliness	All settlement reports and supplementary reports have been published to designated areas before 6pm on publication date	100%	100%	100%	100%
Customer calls/service requests dealt with within SLAs	CGI dealing with queries within contractual SLA	85%	97.7%	99%	97.7%

Comments on KPIs:

We have highlighted our key KPIs which we use to monitor our operational performance. We monitor and report these KPIs to the Board to provide oversight of our performance.

MO Compliance

It is important to us to deliver a compliant operation with the appropriate governance and oversight. We report our compliance quarterly (to trading parties) and are focused on achieving 100% compliance with high impact obligations, 90% compliance with medium obligations and 80% compliance with low impact obligations.

Completion of our work programme with respect to Business Continuity Magement (BCM) and the Market Incident Management Plan (MIMP) and achieving ISO accreditation will mean we are fully compliant with all high impact obligations.

Further details on MOSL compliance can be found here on our website.

Query turnaround

We track the number of queries received from trading parties sent either direct or through our Portfolio Managers. Queries are monitored for responses within the SLA of ten business days.

We are currently performing above this SLA.

Settlement timeliness

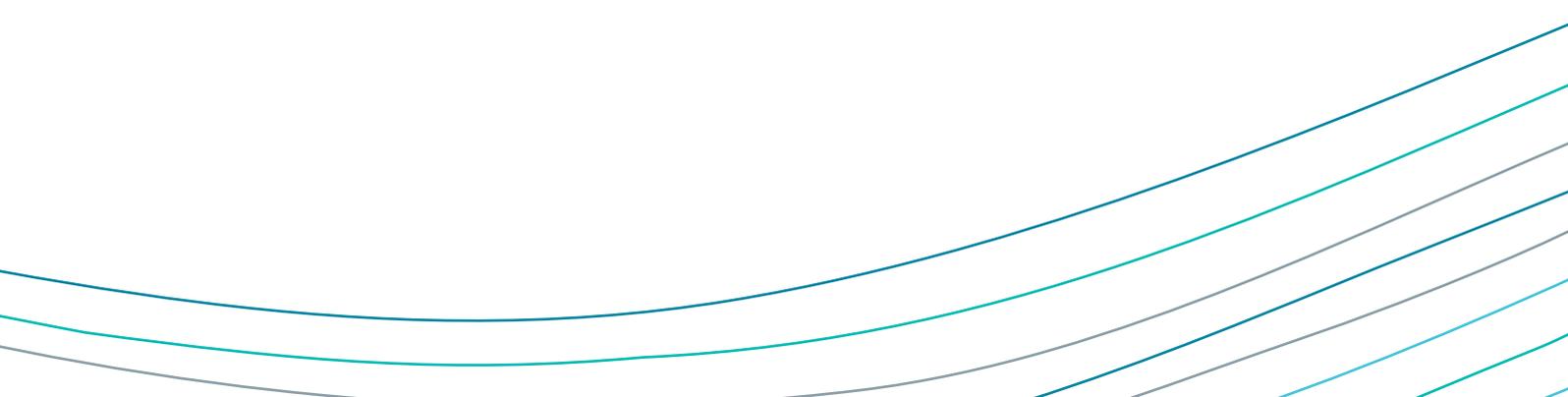
Enabling retailers and wholesalers to get their billing out on time based on accurate settlement reports (based on the data input into CMOS) is critical for the market to operate. We work to 100% compliance of all settlement reports and supplementary reports published to designated areas before 6pm on publication date.

We are currently performing in line with this KPI.

Customer calls / service requests dealt with within SLAs

CGI provide Service Desk support for trading parties in the event they encounter issues with CMOS. The Service Desk is contactable by phone and email and under the contract, CGI are required to respond to these queries within a fixed time period and achieve a service level target of 85%.

CGI are currently performing above this SLA.



Market activity indicators

Market Activity indicator	June	May	April
No. of active retailers in market incl number of retailers currently going through market entry assurance	44 retailers 8 retailers in entry process	42 retailers 7 retailers in entry process	41 retailers 8 retailers in entry process
No. of supply points switched in month	7,288	8,095	7,054
Settlement R1 total settlement value	£209.418m 6 unplanned runs	£214.408m 18 unplanned runs	£206.801m 18 unplanned runs
No. of corrective/unplanned settlement runs and value	£5.58m corrective settlement value	£3.42m corrective settlement value	-£0.42m corrective settlement value
No. of disputes in month by type (and short commentary on nature of/themes of disputes)	4 Trading disputes 1 MAC dispute	3 Trading disputes	2 Trading disputes

Comments on KPIs:

Smarta Water Limited and Blackpool Borough Council both entered the market in June. Utility Bidder Limited entered the market in July, and Tor Water Limited entered the market in August. There are currently seven applicants going through the market entry process.

We continue to see trading disputes being raised to correct ongoing issues between retailers and wholesalers and to enable unplanned settlement runs to occur outside of the current timescales. A MAC dispute was raised by a retailer with MOSL in relation to incorrect MPS charges, however a resolution has been agreed by both parties.

Market Governance Indicator	Description	June	May	April
Change proposal duration from initial submission to implementation (MAA)	Cumulative	94 BDs	94 BDs	79 BDs
Number of Change proposals completed (MAA)	Number of CPs approved by Ofwat	25	22	19
Number of Change proposals in progress (MAA)	Number of CPs in process	13	12	13

Comments on KPIs:

In June, one change proposal was raised by MOSL. CPW037 seeks to remove the Error/Return Code Set table from CSD 0301 Data Catalogue and introduce a reference to a separate document which contains the Error Codes. Three change proposals were approved by Ofwat - CPW026, CPW032 and CPW036.

Currently in the Assessment process, CPM008 seeks to make amendments to the redistribution of charging arrangement currently specified in MAC 9.1.2. There are five Change proposals with Ofwat, which are currently pending an Ofwat decision. There are seven Change proposals which have been approved by Ofwat and are awaiting implementation.



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