

# **Yorkshire Water Credit Support & Alternative Payment Terms Consultation Results**

**October 2019**

# About this consultation

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# 1. Introduction

In April 2019, Yorkshire Water introduced Credit Support 100 (CS100), an Alternative Eligible Credit (AEC) offering which provides £100,000 of unsecured credit support to all contracted retailers operating within the Yorkshire region (subject to eligibility).

Since its launch, 12 retailers have successfully signed CS100 agreements, and continue to enjoy the benefits of this arrangement. However, Yorkshire Water are keen to explore new and innovative ways in which to support effectively operating markets and following CS100's implementation, committed to further reviewing our approach to credit in the non-household water retail market.

We have now completed our review and have developed a number of additional options which not only complement but enhance our already successful AEC offering to retailers operating in Yorkshire.

As part of this work, we were keen to engage with key stakeholders, with a view to obtaining feedback on our proposals. In August 2019, we published a market wide consultation requesting participation from retailers, wholesalers, Ofwat and MOSL.

Please see below a list of the questions which were included in the consultation, along with a summary of the feedback.

Number	Question
Q1	Please state which organisation you represent?
Q2	How do you think the Yorkshire Water Alternative Eligible Credit Support proposal compares to other Schedule 3 arrangements which are currently operating in the market?
Q3	How do you think the Yorkshire Water Alternative Payment Terms proposal compares to any other Alternative Payment Terms proposals you may have reviewed?
Q4	How do you think the Yorkshire Water Alternative Eligible Credit Support and Alternative Payment Terms proposals will benefit the market?
Q5	If any, which of the objectives and principles of the WRC do you think the Yorkshire Water Alternative Eligible Credit Support and Alternative Payment Terms proposals support?
Q6	Please provide your comments on the draft Alternative Eligible Credit support three-tiered approach and Alternative Payment Terms proposals.
Q7	Would you be interested in requesting an Alternative Eligible Credit agreement and or an Alternative Payment Terms agreement based on these proposals? If No, please explain why not.
Q8	Is the Alternative Payment Terms worked example included in the consultation easy to understand?

## 1.2 Responses

A total of 6 respondents participated in the consultation and there was a positive mix of retailers and wholesalers.

We are pleased to report that the majority of the feedback received was positive, however we did receive some valid and constructive feedback, which we have utilised to further enhance our initial proposal.

Further to this feedback, we have identified that whilst our three-tiered approach is innovative and aims to provide a structured and risk based credit allowance framework, there is more for us to consider. This is particularly in how we negotiate AEC with retailers who are deemed to be financially stable and secure, but do not meet the Investment Grade requirements.

With this in mind, it is our intention that we will continue to develop our risk-based framework and we look forward to engaging with key stakeholders to help us in this regard.

# Consultation Results

## 2. Results

### How do you think the Yorkshire Water Alternative Eligible Credit Support proposal compares to other Schedule 3 arrangements which are currently operating in the market?

Two thirds of respondents provided a positive response to this question. Comments such as “it is one of the best”, “a very positive move” and “commendable” provide us with confidence that the three-tiered approach has been well received and is deemed to be beneficial. There was also recognition that whilst there are some similarities to other similar arrangements already operating in the market, the Yorkshire Water three-tiered approach “offers greater flexibility”.

One respondent provided an opinion that the proposal could potentially hinder competition if “payment performance metrics” are not considered as a means by which to provide enhanced levels of unsecured credit. Whilst we welcome this feedback, it is the view of Yorkshire Water that payment performance is already accounted for within the market codes, specifically Schedule 2E of the Business Terms, which determines that a retailers unsecured credit allowance is calculated based upon its credit rating (Key Terms (5)).

The Yorkshire Water three-tiered approach seeks to utilise a similar risk-based approach as the Market Codes when determining the enhanced levels of unsecured credit which may be offered to retailers i.e. demonstrable evidence of financial stability and payment performance is to be provided in order to assess and the financial risk imposed upon YW.

Our extensive analysis determined that Government backed organisations, along with those organisations who hold an Investment Grade Credit Rating, pose less of a financial risk than organisations which do not. It is this logical risk-based approach which led us to the decision that it would be beneficial to build upon the existing Market Codes by extending further unsecured credit to those market participants who meet the Investment Grade Credit rating or are Government owned

The same respondent also commented that the three-tiered approach was only of benefit to larger retailers and therefore may be anti-competitive. However, our proposal will retain the CS100 offering which is open to all retailers large or small. The additional suite of arrangements included within our proposal simply seeks to provide a broader range of unsecured credit options to retailers who may hold a stronger financial position. We are therefore confident that providing unsecured credit via a tiered risk-based approach enables YW to provide excellent unsecured credit facilities to retailers, whilst ensuring that we operate as a responsible wholesaler by carefully managing our financial risk exposure.

### How do you think the Yorkshire Water Alternative Payment Terms proposal compares to any other Alternative Payment Terms proposals you may have reviewed?

Most respondents were unable to make a comparison to any other Alternative Payment Terms operating within the market, as there are yet to be any agreements formally published. Whilst most respondents were not able to provide specific feedback on any possible improvements, Yorkshire Water are pleased that we are the first wholesaler to publish Alternative Payment Terms, as this meets our objective of supporting successful and competitive markets through innovation.

One respondent did provide the following comments; *“the qualification criteria of Government backed or ‘retailer’ investment grade (cl. 1.2.4) fails to recognise current credit arrangements where credit*

*guarantees from an investment grade financial institution provided by a retailer are acceptable for post pay eligibility. As such there is no differential in risk between such guarantees being provided by a retailer without an investment grade and a retailer with investment grade. Therefore, as a minimum, the definition should be amended to expand the eligibility criteria to align with credit arrangements currently acceptable for 50 days”*

We welcome this feedback which we have carefully considered. We agree that the Alternative Payment Terms 90 (APT90) eligibility criteria should be amended to reflect that of the Market Codes. We are therefore pleased to confirm that we have removed the requirement for a retailer to hold an Investment Grade Rating, or have Government backed ownership status to be eligible for our Alternative Payment Terms offering.

### **How do you think the Yorkshire Water Alternative Eligible Credit Support and Alternative Payment Terms proposals will benefit the market?**

All respondents provided positive feedback regarding wholesalers continuing to provide more flexibility and a greater range of options regarding credit in the market.

*One respondent said “The Eligible Credit Support will result in greater liquidity in the market, it will enable more switching and ease the barriers to entry, whilst limiting risk to a reasonable level. The three levels of support are fair and reasonable and offer appropriate credit support across the whole range of retailers. Linking these Credit Support options to good payment history is fair and will encourage prompt payment which is beneficial to the whole market and reduces risk for Yorkshire Water”*

Two respondents also associated the working capital benefits brought about by Alternative Payment Terms, directly to tangible customer benefits which will result in lower and customisable customer bills. From a YW perspective, we see this feedback as confirmation that we have achieved one of our objectives of supporting an effective, competitive water retail market by reducing customer bills.

One respondent reiterated their comments regarding the three-tiered approach potentially impeding competition due to larger retailers receiving more economic benefit than small retailers due to the favourable structures of some larger companies. Whilst we acknowledge this feedback, we believe that the additional suite of arrangements included within our proposal simply seeks to provide a broader range of unsecured credit options to retailers who may hold a stronger financial position. We are therefore confident that providing unsecured credit via a tiered risk-based approach enables YW to provide excellent unsecured credit facilities to retailers, whilst ensuring that we operate as a responsible wholesaler by carefully managing our financial risk exposure.



## If any, which of the objectives and principles of the WRC do you think the Yorkshire Water Alternative Eligible Credit Support and Alternative Payment Terms proposals support?

### Retailer Comments

- it is efficient as it delivers what it aims to deliver effectively
- it is proportional as a reasonable balance of risk is maintained, the inclusion of good payment criteria also helps reduce the risk to Yorkshire Water
- it is very simple and secure, and it has imposed no additional costs on us
- it reduces barriers to entry as it enables new entrants to get a foothold in the market
- it is open to all who meet the criteria, so it is non-discriminatory, the three levels mean that there is access to appropriate credit across the whole range of retailers.

We have no experience of how it impacts on the other objective and principles of the WRC, but that doesn't mean it does not have benefits in these areas.

The alternative credit support fits the following objectives Simplicity, cost effectiveness, security and barriers to entry.

We do not believe the alternative payment terms fits the objectives and principles of the WRC

Other than transparency, none as currently proposed.

Barriers to entry & Non-Discrimination.

Several. Primarily though, both APT and AEC lower barriers to new market entry, in that lower capital investment is required by Retailers with less trading/ credit history, or who are not supported financially through a larger group/ have less access to parental guarantees.

All core principles of the WRC have been captured. We note that both proposals have been set out to achieve the appropriate outcomes for all retailers of differing sizes and structures.

## Please provide your comments on the draft AEC three-tiered approach and APT proposals.

Two respondents reiterated their previous positive comments regarding their appreciation for Yorkshire Waters continuing commitment to review and enhance already successful proposals which extend beyond its obligations as detailed in the Market Codes.

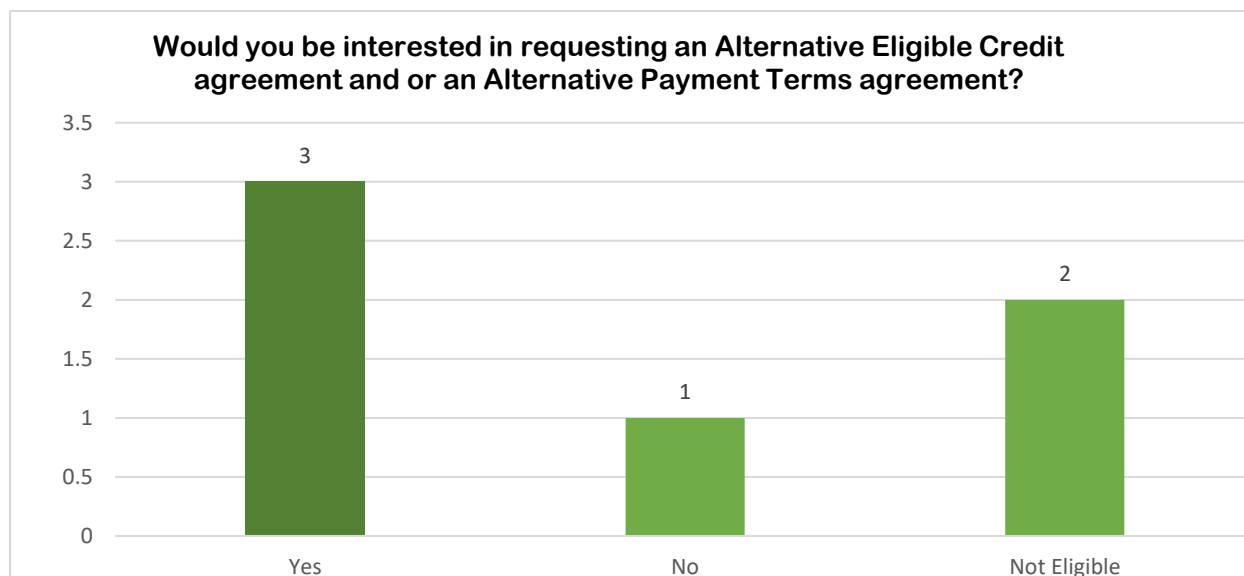
One respondent provided no further comments and one confirmed that they had not reviewed the detailed agreements.

Another respondent commented that “the three-tiered approach is only beneficial to larger retailers”. Whilst we appreciate that it is more likely that retailers who hold an Investment Grade Credit rating, or are Government owned are generally likely to be larger retailers, as previously confirmed, the YW CS100 offering remains in place and complements CSIG and CSGOV by providing a £100,000 unsecured credit facility to all retailers regardless of size or time in spent operating in the market.

We also received comments from one wholesaler who was concerned that the APT90 proposal may be damaging to their organisation. The wholesaler commented that if the APT90 was requested by all retailers operating in their area, then this would require them to procure additional financing in order to bolster their working capital funds. Clearly Yorkshire Water have and will continue to consider the

potential implications on other market participants prior to launching initiatives such as this, however we believe that all wholesalers must undertake their own financial risk assessment prior to accepting a request for Alternative Payment Terms.

Yorkshire Water have undertaken extensive financial modelling prior to the publication of this consultation and have concluded that we are able to increase retailer's payment terms to 90 days without introducing any additional risk to our business. We appreciate that some wholesalers may not be in a position financially to offer such an initiative in their area of appointment, however we do not see the implementation of APT90 in Yorkshire as negatively impacting any other market participants.



### Is the APT90 worked example included in the consultation easy to understand?

100% of respondents confirmed that the proposals and the worked examples were clear and easy to understand.

### Please provide any further feedback you may have regarding this consultation.

Of the respondents completing this question, the feedback was generally consistent with their feedback provided throughout the previous questions.

There was however one respondent who provided the following comments *"It should be noted though these Similar schemes have moved away from imposing the "Investment Grade - Minimum Credit Rating" as the main eligibility criteria having found this to still act as an obstacle in that it ignores the fact that the required investment-grade status will not always be held by the part of the business that holds the water licence"*

Following this feedback and further discussions internally, we recognise that that CSIG may not meet the needs of some organisations due to the structure of their business, despite the fact that their group of businesses may hold an Investment Grade rating.

We therefore commit to conducting a further review of our Alternative Eligible Credit offering with a view to identifying further enhancements which take into consideration the feedback received.

# Conclusion

### 3. Conclusion

Following our appraisal of the feedback we have received in response to this consultation, we would like to confirm that it is our intention to launch the Yorkshire Water Three-tiered Credit approach with effect from 13th September 2019. We will write to all market participants directly to inform them that Credit Support 100, Credit Support Investment Grade, Credit Support Government and Alternative Payment Terms 90 are available on the Yorkshire Water website..

We would also like to confirm for clarity that, in response to the feedback received as part of this consultation, we have made the following changes to our proposal;

- We have amended the eligibility criteria which requires retailers to hold an Investment Grade Credit rating in order to take advantage of Alternative payment Terms 90

In addition to the above change, we would also like to share with you the following commitment;

- Yorkshire Water will continue to review its current Alternative Eligible Credit offering, with a view to identifying further innovative solutions in order to support and encourage an effective and competitive water retail market. We will conclude this review and communicate the outputs before the 31st March 2020. Additionally, we look forward to supporting and contributing towards future market led developments in this area.

We would like to take this opportunity to thank those of you who participated in this consultation, your feedback has been invaluable and has helped us to refine our proposal. We also hope those of you who have taken the opportunity to review the consultation feedback have found it useful.

#### Useful Links

Credit Support 100: <https://www.yorkshirewater.com/media/1497/schedule-3-credit-support-100-edit-blank-boxes-v2.pdf>

Credit Support Gov: [https://www.yorkshirewater.com/media/1805/schedule-3-credit-support-gov\\_for-publication.pdf](https://www.yorkshirewater.com/media/1805/schedule-3-credit-support-gov_for-publication.pdf)

Credit Support Investment Grade: [https://www.yorkshirewater.com/media/1804/schedule-3-credit-support-ig\\_for-publication.pdf](https://www.yorkshirewater.com/media/1804/schedule-3-credit-support-ig_for-publication.pdf)

Eligibility Criteria: <https://www.yorkshirewater.com/media/1803/yorkshire-water-aec-apt-eligibility-criteria-v4-for-publication.pdf>

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