



Water Services Regulation Authority Water Industry Act 1991 Section 8(3)

Proposal by the Water Services Regulation Authority (Ofwat) to vary the appointments of SSE Water and Dŵr Cymru Cyfyngedig as water and sewerage undertakers.

This notice is a consultation on this proposal. The consultation period will last for 28 days. Having considered any representations submitted in response to the consultation, a committee of Ofwat's Board will decide whether or not to grant the variations to these companies' appointments.

The Site

SSE Water has applied to be the water and sewerage company for a development consisting of 4000 household properties called Coed Darcy, Llandarcy (the Site). The Site is presently within the water supply and sewerage services areas of Dŵr Cymru.

The proposal

Ofwat proposes to:

- (i) vary the appointment of SSE Water as a water and sewerage company by adding the Site to its water supply and sewerage services areas; and
- (ii) vary the appointment of Dŵr Cymru as a water and sewerage company by excluding the Site from its water supply and sewerage services area.

By means of these variations, SSE Water will become the water and sewerage supplier for the Site.

Policy for new appointments and variations

The new appointment and variation mechanism, set out in primary law¹, provides an opportunity for entry and expansion into the water and sewerage sectors by allowing one company to replace the existing appointee as the provider of water and / or sewerage services for a specific area. This mechanism can be used by new companies to enter the market and by existing appointees to expand their businesses.

When considering applications for new appointments and variations, Ofwat operates within the statutory framework set out by Parliament, including our statutory duty to protect consumers, wherever appropriate by promoting effective competition. In particular, in relation to unserved sites, we consider that we must ensure that the future customers on the site – who do not have a choice of supplier – are adequately protected. When assessing applications for new appointments and variations, the two key policy principles we apply are that:

1. customers, or future customers, should be no worse off than if the Site had been supplied by the existing appointee; and
2. Ofwat must be satisfied that an applicant will be able to finance the proper carrying out of its functions as a water and/or sewerage company.

We clarified these two policy principles in February 2011 when we published our 'New appointments and variations – a statement on our [policy](#) and [process](#) for new appointments and variations'.

When we assess whether customers will be no worse off as a result of the appointment, we not only consider the customers on the site but also the generality of customers. These include not only the customers of the existing provider but also customers more generally across England and Wales, who in our view benefit from the effective operation of the new appointment and variation mechanism.

¹ The legal framework for new appointments is set out in the Water Industry Act 1991 (WIA91). Section 7 of the WIA sets out the criteria by which an appointment or variation may be made. Section 8 sets out the procedure for making that appointment or variation.

The application

SSE Water has applied to be the water and sewerage company for the Site under the unserved criterion set out in section 7(4)(b) Water Industry Act 1991.

Unserved status of the Site

To qualify under the unserved criterion, an applicant must show that at the time the appointment is made, none of the premises in the proposed area of appointment is served by the existing appointee. We have received an independent report that verifies the site as being unserved. The report was shared with Dŵr Cymru and Dŵr Cymru has confirmed that it agrees that the site is unserved.

Protecting customers

Ofwat acts to protect consumers, especially those who are unable to choose their supplier. In assessing applications to supply new development sites, Ofwat acts on behalf of end-customers who are not yet on site to protect their interests. The fact that future customers on the Site have not directly chosen SSE Water to be their supplier is not a position unique to new appointments – very few customers in England and Wales are able to choose their supplier².

Recognising this, our assessment of applicants' proposals includes analysis of their plans to ensure customers will be at least no worse off in terms of their annual bills and levels of service than if they had been supplied by the existing appointee. We will continue to protect customers on the Site by regulating the new appointee's prices and service levels.

Customers on the Site – price

SSE Water will take a bulk supply of water from Dŵr Cymru to supply the Site, and will discharge from the Site into Dŵr Cymru's sewers.

² The only customers that can choose their supplier are non-household customers that consume at least 5MI per year and are supplied by a company that is wholly or mainly in England (and at least 50MI for companies wholly or mainly in Wales) and satisfy the Water Supply Licensing (WSL) eligibility criteria. Those non-household customers that consume at least 50 MI in England (and at least 250 MI in Wales) can switch under either the WSL or NAV regime.

SSE Water will match the existing metered water and sewerage household tariffs. SSE is not offering a discount on these tariffs. The WaterSure tariff will be available to those customers that apply and qualify for it³.

Having considered SSE Water's pricing proposals, we are satisfied that customers will be at least no worse off in terms of their annual bills than if they had been served by Dŵr Cymru.

Currently, SSE Water's conditions of appointment provide that SSE Water's price limit is set by reference to the charges of the previous appointee for each of its sites. In this case, SSE Water may not charge customers on the Site more than Dŵr Cymru's charges for water and sewerage. We consider that, given SSE Water's small size, this represents a more proportionate way of regulating its prices than subjecting it to a full bespoke price review as we do for larger companies. However, condition B of SSE Water's conditions of appointment allows us to set a specific price limit for SSE Water. This condition is temporarily suspended but we will activate it when we consider it is appropriate to do so. This is unlikely to be before 2014.

Customers on the Site – levels of service

SSE Water will be subject to the same customer service level requirements as other water and sewerage appointees.

Guaranteed standards scheme (GSS) compliance and base service levels

SSE Water has submitted information about its proposed service levels under:

- the statutory requirement of the GSS Regulations;
- our service indicators; and
- its own company standards.

We have assessed these planned levels of service and are satisfied that they match or exceed those typically achieved by Dŵr Cymru and the sector as a whole.

³ Through the WaterSure scheme, households on meters who receive certain means tested benefits or tax credits, and are either responsible for three or more children under the age of 19, or have a medical condition which requires significant additional use of water, can apply to pay no more than the average household bill for their region.

Codes of Practice

Every appointee is required under conditions G, H and I of its conditions of appointment to publish debt, leakage and customer Codes of Practice. We have assessed SSE Water's Codes of Practice, and are content that these are of an approvable standard and that customers on the Site would be no worse off than if they had been served by Dŵr Cymru. The Consumer Council for Water, the independent public body that represents water and sewerage consumers in England and Wales, is also content with Ofwat's assessment of SSE Water's Codes of Practice.

SSE Water's voluntary standards

We have also made a detailed check of SSE Water's voluntary service standards, including where they enhance the statutory GSS provisions, as part of approving SSE Water's Codes of Practice. We require that SSE Water matches or exceeds Dŵr Cymru's own standards (except where there is reasonable justification for not doing so).

Examples of where SSE Water will offer improved customer service compared with Dŵr Cymru include:

- SSE Water will offer an unlimited number of free leak repairs to domestic customer supply pipes, as compared with Dŵr Cymru which only offers a single leak repair for each domestic property every three years. (However, for a new build site leakage should be less likely which makes it an easy option for SSE Water to offer an improved policy).
- SSE Water offers to check domestic customer meters for free, as well as offering an independent test which has a charge if the meter is found to be working within acceptable limits. Dŵr Cymru only offer the independent test.
- SSE Water's call centre opening hours are at least as good as Dŵr Cymru (Dŵr Cymru offers 8am-8pm Monday to Friday and 8.30am-1.30pm on Saturday, whereas SSE Water offers 8am-8pm Monday to Friday and 8am-2.00pm on Saturday. Both have 24-hour lines for emergencies).
- SSE Water will make higher GSS payments in some areas, for example offering £50 for low pressure or failing to respond to account queries within 10 days, compared with Dŵr Cymru £25 and £20 respectively.

- SSE Water offers several additional standards which Dŵr Cymru does not offer. For example, it will pay £100 for internal flooding due to a burst water main, £30 if it does not read a customer's meter at least once a year and £20 if a special assistance application is not processed in five days.

However, SSE Water does not propose to match Dŵr Cymru in some ways, for example:

- SSE Water does not offer as extensive a range of payment options, although the range it does offer is adequate. SSE has signalled its intention to expand this range in future.
- SSE Water offers more limited ways for customers to contact it than Dŵr Cymru. For example, Dŵr Cymru has a 24 hour automated bill payment line, and has a live web chat function with customer service agents.
- SSE Water does not currently have an assistance fund, but Dŵr Cymru does. However, several other incumbents do not offer an assistance funds.

Whilst the areas in which SSE Water does not propose to match Dŵr Cymru are not statutory or appointment requirements, we have explained to SSE Water that these areas must be kept under review as its customer base expands. SSE Water has committed to do so. As a minimum, we will review these three years after the most recent approval as part of the re-approval of Codes of Practice. As SSE Water extends into different existing appointees' areas, all Codes will be assessed against other existing appointees' policies and we will request improvements we judge are required as its customer base grows.

Having considered SSE Water's overall proposed service levels, and compared them with those of Dŵr Cymru, we are satisfied that customers on the Site will receive a level of service that is comparable with the level of service they would have received had they been served by Dŵr Cymru.

Dŵr Cymru's existing customers

In considering whether customers will be no worse off, we also considered the potential effects of this variation on the prices that Dŵr Cymru's existing customer base may face.

We have looked at this potential impact by comparing how much Dŵr Cymru might have expected to receive in revenue from serving the Site directly, with the revenues they might expect from serving the Site indirectly via bulk supply and discharge agreements with SSE Water. The calculation necessarily depends on a range of assumptions about what revenues **might** have been received and incurred, and what the customer base in Dŵr Cymru's area **might** have been if they had supplied the Site. There are clearly difficulties involved in quantifying the effect on Dŵr Cymru and it is necessary to use a simplified set of figures. We have expressed the effect in 'per bill' terms to try and quantify the possible effect in an easily understandable way.

We believe the upper bound of the **potential** effect amounts to approximately a £0.50 increase per annual bill for each of Dŵr Cymru's billed customers when the Site is fully built in 2026.

Dŵr Cymru's customers will not, therefore, automatically see their bills increase by this amount. It is important to note, this £0.50 increase per annual bill takes no account of the following:

- The potential cost savings by Dŵr Cymru from dealing with SSE Water as a single customer for the Site rather than 4000 individual customers. Or;
- The offsetting of the additional benefits to all customers that arise from the new appointments mechanism.

In this case, we consider this potential effect is outweighed by the benefits of granting this variation. We set out the wider benefits we believe stem from the new appointments and variations regime below.

Developer choice

Ofwat takes into consideration the choices of the site developer. In this case, the Site developer has said that it wants SSE Water to be the water and sewerage company for the Site.

Environment Agency (EA) and Drinking Water Inspectorate (DWI)

We take the views of these organisations into account before progressing to consultation on an application for a new appointment. Both EA and DWI informed us that they are content for us to consult on this application.

Wider benefits

The new appointment and variation mechanism provides a means for companies from outside the water and sewerage sectors to enter the market and for existing water and sewerage appointees to expand their businesses.

Entry and expansion (and even the threat of such by potential competitors) can lead to benefits for different customers in different ways (such as developers of new housing sites and household and non-household customers). Examples of benefits delivered via the new appointment and variation mechanism include price discounts, better services, environmental improvements and innovation in the way services are delivered. Benefits can also accrue to the existing appointee's customers, because when that appointee faces a challenge to its business that challenge can act as a spur for it to raise its game.

These wider benefits that we believe stem from the new appointments and variations regime are set out more fully in our [policy statement](#).

Overall assessment of effect on customers

Overall, we consider that customers on the Site will be at least no worse off served by SSE Water than they would have been had they been served by Dŵr Cymru. We consider that the potential effect on Dŵr Cymru's existing customers is very likely to be offset by the wider benefits of the new appointment and variation mechanism. We are therefore satisfied that customers would be no worse off as a result of our granting this variation.

Ability to finance the proper carrying out of functions

We have a statutory duty to ensure that efficient appointees can finance the proper carrying out of their functions. When a company applies for a new appointment or variation to serve a site we therefore consider the financial position of the appointed company as a whole (which may include other areas of appointment) and the financial position in respect of the specific site.

We assess this by taking a risk-based approach to assessing the viability of the individual site, to ensure that each new appointment and subsequent variation to that appointment carries a low risk of being financially unviable. As a new appointee's business is made up of these collective variations, in this way we ensure as far as possible that the new appointee will be able to finance the proper carrying out of its functions.

We have conducted these assessments in respect of SSE Water's application to serve this Site and are satisfied that the risk of this Site being financially unviable is at an acceptable level.

Conclusion and next steps

In assessing SSE Water's application for this variation, we have considered the general benefits of new appointments. We are satisfied that our two key policy principles have been met in this case, as customers will be no worse off, and SSE Water will be able to finance its functions.

We have also considered the effects of granting this variation on Dŵr Cymru's existing business and the approximate increase of £0.50 per annual bill for each of Dŵr Cymru's billed customers. However as noted above, we consider this potential effect is outweighed by the benefits of granting this variation and Dŵr Cymru's customers will not automatically see their bills increase by this amount in any event.

We are therefore minded to grant the appointment under the unserved criterion. We are consulting on our proposal to do so.

Where to send submissions

Any representations about, or objections to, this proposal should be sent in writing to Claire Simpson, Senior Case Officer, Markets and Economics Division, Ofwat, Centre City Tower, 7 Hill Street, Birmingham, B5 4UA so as to be received no later than 27 September 2012. Submissions can also be emailed to: claire.simpson@ofwat.gsi.gov.uk.