



South Staffs Water

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Retail Licensing,
Ofwat,
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By email to retaillicensing@ofwat.gsi.gov.uk

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Dear Sirs,

South Staffs Water is pleased to submit our response to the Ofwat consultation on retail licensing. We have structured this response in accordance with the questions within the consultation.

Q1 Do you agree with the proposal to have separate licences covering water and wastewater retail? If not, please explain how you envisage that a single licence for water and wastewater would differ?

We agree that the modular license approach is sensible and allows a retailer to choose whether to be active in the water, wastewater, or both, markets. However where a retailer wants to compete in both markets, we would expect that the process for application for both licenses simultaneously would not be any more onerous than applying for one of the licenses (we would expect to make a single joint application for both licenses rather than two separate applications, to avoid duplication of effort).

Q2 Do you agree with the proposed amendments to standard conditions for the new water supply and sewerage service licence (WSSL)?

We agree with the proposed amendments.

Q3 Do you think any of the proposed amendments listed in Table 2 are non-routine and require additional discussion? If so, why?

We have no further points to raise on the amendments listed in Table 2.

Q4 Do you agree with the proposed approach to maintaining customer protection in the future WSSL?

We agree with the proposed reworking of the Certificate of Adequacy guidance and the principle that stakeholders need assurance on the competency of a new retailer. There may come a time when the market has matured and no longer needs this assurance.

Q5 Do you agree with the proposed approach to Market Arrangements Code enablement?

We agree with the proposed approach and to the inclusion of an additional license condition in both the WSSL and the Instrument of Appointment.

Q6 Do you have any specific comments on the legal drafting?

We suggest that the legal drafting is considered as a final step once the intentions are fully agreed through the consultation and subsequent workshops. Discussions in the initial workshop showed this to be an area that could overwhelm the substance of the discussions. For this consultation response, we have focussed on the principles of the document rather than the legal drafting.

Q7 Do you agree with the proposed approach to include requirements on arm's length transactions and non-discrimination?

We agree with the proposed approach as maintaining equivalence for all participants should be a key requirement, and therefore belongs in the WSSL.

Q8 Do you have any other comments on our proposed conditions in this area?

We have no further comments.

Q9 Do you have any other observations about our proposals on changes to the standard conditions for the new Water Supply Licence?

We would like to note that the exit regulations, yet to be finalised, may have impacts or cross over to the WSSL.

Q10 Are there any areas not covered in the proposals in which you consider changes are required?

Section 5 in the proposed license drafting (appendix, page 8), lists circumstances where the licensee must comply with the instructions of the undertaker; we have

observed that there is no similar condition where the licensee must comply with the undertaker's instructions in the situation of leaks on premises, defective fittings or non-compliance with water fittings regulations. We would like to suggest that these areas, for which undertakers currently have enforcement powers, should be considered as to whether there needs to be any coverage in the retail licenses.

Q11 Do you agree with our proposals for the conditions within Table 4? Please respond separately on each of the three Appointment conditions (Q, G and I) discussed.

In general the process for retailers claiming allowances has been set out in part H of the Operational Terms. We think that this section of the code should be expanded to include all possible allowances, including the condition Q and I elements below and also GSS when this detail is known. Currently supply interruptions for drought sits in Business Terms section 2, and we are unsure why this is treated differently to other allowances.

On condition Q

We have no objection to the removal of references to non-household customers from condition Q of our license, as it will now be covered under the codes. However we have two concerns:

- How is the customer protected from retailers failing to pass this on or not passing it on in full, particularly in the case of business failure?
- The detail on GSS (schedule 3), which the supply interruptions drought compensation payment refers to, is not yet available. We would reserve our final position on this until the full detail is available.

On condition G

We agree that the Operational Terms do need to include the requirement for the retailer to inform the customer about the process for escalating complaints to CCWater.

On condition I

We would look to ensure that changes to this condition do not create additional obligations over those which already exist in our current license conditions.

Q12 Do you agree with our proposals for the conditions within Section 5.1.2 on equivalence? Please respond separately on each of the eight conditions discussed.

Condition F6 – Agreed

Condition F6A2A – Agreed

Condition R1-3 – Agreed

Condition R5.1 – Agreed

Condition R5.3 – No concerns if this is removed

Condition R7-9 – OK to amend or delete

Condition S – OK to amend or delete

On condition N

The license fee as part of condition N is currently apportioned across wholesale, HH retail and NHH retail. In principle we have no objection to a license fee being levied on NHH retail to obtain equivalence, but we have the following comments:

- We would expect that the fee applied to the non-exited NHH retail element is an appropriate reapportionment of the current total fee within the regulated price controls – not an additional or new fee on top of the current fees.
- As NHH customers switch away from default tariffs and therefore away from the non-exited retailer to the WSSL retailer, then how does the fee proportionally reduce in line with how the NHH revenues will reduce under the proposed true up mechanisms being developed?
- We wonder whether having a separate fee for non-exited NHH retail will provide any equivalence benefits in reality, since the default tariffs under the non-exited retail NHH will still be regulated, so in that sense the business model for this particular price control element is not similar to the commercial retail WSSL held separately for participation in the market.

Q13 Do you agree with the draft condition set out in Appendix A to enable the Market Arrangements Code? Are there any reasons why this condition should differ between the Appointment and the standard conditions of the WSSL?

We agree with the inclusion of the MAC condition in appendix A. At this stage we cannot see any reason for variation between the Instrument of Appointment and the WSSL.

Q14 What are your views on the proposed 'stapling' condition set out in Appendix B requiring the company to adhere to the Wholesale Retail Code in its interactions with its own retail business? Does the proposed condition work alongside Schedule 8 of the Market Arrangements Code?

We are happy that the principle of the stapling condition will cement the obligation for a company to adhere to the codes within its license. We have not examined the detailed legal drafting.

Q15 Do you consider that the proposals will achieve the objective of equivalence, with the same obligations and opportunities for all retailers? If not, what additional suggestions do you have?

We think that the proposals are a good start. There may well still be gaps, which will most likely not be apparent until the market is actually in operation as many day to day activities cannot be covered explicitly by high level license clauses. Future modifications can be addressed through changes via the Codes Panel and can be identified as part of market operation.

Q16 Do you have any other observations about our proposals on changes to the conditions for the Instruments of Appointment?

We have no further comments to make in addition to our responses to previous questions.

Q17 Are there any areas not covered in the proposals in which you consider that changes are required?

We have no further suggestions.

Q18 Are there any areas in your Appointment in which you think differences from the examples used will require detailed consideration in future work?

We are not aware of any differences at this time, although we will need to further examine the legal drafting as it develops.

Q19 Do you agree that we should retain the three basic elements of financial stability, managerial competency and technical competency in assessing future licence applications?

We agree with the current three basic elements and think they represent an appropriate level of checks for license applications.

Q20 Do you agree that gaining a retail future WSSL licence should be conditional on successfully completing market accession testing? Are there any aspects of the licensing process that could be further simplified to avoid duplication/overlap across the two processes?

We believe that demonstrating that a new retailer can effectively interact with the market operator is fundamental to being able to operate in the market. Any current licensees should be subject to the same test. We are keen that the overall process is smooth and time efficient.

Q21 Do you have any comments on the proposal that licence applications for the future market should include the provision of a completed certificate of adequacy?

We agree that the certificate of adequacy forms an important assurance stage in the early days of the market. However we suggest that as the market develops the need for a certificate of adequacy may reduce, and reviews of the overall process in the future will determine if that is the case.

Q22 Do you have any comments about the coverage of wastewater in the licence application process and the role played by the Environment Agency?

There is an appropriate balance to be struck between protecting customers and creating barriers to entry. We consider that the requirement for technical competency as part of the three basic elements of the Certificate of Adequacy will ensure that any new retailer will have met the required technical knowledge of both water and wastewater retail activities and customer services. We have no objection to the license application including some additional questions on wastewater matters since this will cement the requirement on technical competency and help to ensure that new retailers avail themselves of the appropriate knowledge base.

Where the EA has specific technical requirements regarding wastewater, we would expect these to be easily available in a form which is understandable by any new entrant to the wastewater market, so as not to create a burdensome barrier to entry.

Q23 Do you consider that the role of any sponsor should be maintained, limited or removed entirely? What are your reasons for this view?

Given the limitations inherent within the assurance processes that any sponsor may use, we are not clear what value a sponsor adds. If a business is not financially viable then it should not be allowed entry, and as Ofwat point out, a sponsor makes little difference to this assessment given the lack of incentive on the sponsor to thoroughly assure this.

The consultation states that a sponsor cannot be a related undertaker, but also states that a sponsor can be a financial backer. Does this mean that a sponsor can be the parent company of a retailer where that company is also the parent of the water undertaker?

Q24 Do you have any comments about the proposals to include coverage of customer facing systems in the managerial competency tests?

We believe that including customer facing systems in the competency tests could be overly burdensome, and we are unsure on what criteria a new entrant could be judged on for its customer facing systems. The competitive market itself will dictate the level of customer facing systems that retailers need or offer and the market will find its own level.

Q25 Do you agree that the scale considerations are better dealt with via the certificate of adequacy rather than additional testing in the licence application process?

We appreciate the difficulty in trying to assess, up front, a new retailer's capacity for large or sudden jumps in scale. Whilst the certificate of adequacy is a pre-requisite for a license, we do not necessarily think that it should be an ongoing process once

an established business is trying to increase its market share. A sensible business would not try to grow beyond its ability to service, and if service began to suffer because of this occurring, then in a competitive market we would expect those customers to switch away from the retailer giving them poor service.

However in the exit situation, or acquisition of a large number of customers from another retailer, then in that case we would expect that some regulatory assurance should be provided to ensure that the retailer can absorb that step change, and in that case a refreshed certificate of adequacy would seem an appropriate mechanism.

Q26 Do you agree with our proposed transition approach for current retail only WSL?

We agree with the proposed approach.

Q27 Do you agree with our proposed approach to transition current combined supply WSL?

We agree with the proposed approach but we are keen that the transition does not prevent applications in the interim, and that the process is simple and efficiently administered. The process should not delay access to requirements such as testing.

Q28 Do you agree with our proposed approach for creating self-supply licences?

We wonder whether there should be some minimum thresholds applied to self-supply licenses in order to prevent a situation where there could be many self-supply licensees all supplying themselves, which we think would effectively push retail type costs back onto the wholesaler. Although we acknowledge there are still barriers to entry into the self-supply market, these are significantly reduced compared to a full WSSL licensee. In other words, a high number of self-supply licensees could amount to a very large administrative burden for wholesalers, in the absence of an intermediate retailer.

We also have some concern about high debt risk (to the Wholesaler) in the case of self-supply licensees and how this might be managed.

Q29 Do you agree that there should be a new condition in current licences and Instruments of Appointment to underpin the required preparations?

We are not clear what extra value such a condition would add as existing undertakers have all accepted their obligations in preparation for April 2017 and all companies have engaged thoroughly with the OpenWater programme so far. The assurance milestones in the run up to 2017 should be able to provide the necessary confidence that companies preparations are going to plan, or not, and will allow

Ofwat to engage directly with companies that have potential shortfalls in their preparations. We believe that the various stakeholders working together will be the route to successful preparedness rather than a legal condition in the Instrument of Appointment.

Q30 If you agree that there should be a condition, should it cover both a general obligation and a specific link to a formal transition plan?

As stated above, we do not agree there should be a condition.

Q31 Are there any additional provisions that you think it would be helpful to include in a licence condition on company readiness or any other comments/concerns you would make?

We have no suggestions for additional provisions.

Q32 Do you consider that implementing an auction style allocation process similar to the one that Ofgem has adopted ahead of a backstop allocation process would be the best approach to protecting customers in the event of the failure of a retailer?

We accept that this approach has precedents in the gas and electricity markets, and ensures that the customer has a retailer. We have some concerns that there could be negative consequences on the level playing field in these situations, and also that it does not facilitate a seamless operation between the Scottish and English markets.

Q33 Do you have any suggestions about the best approach to ensuring that the new market arrangements are proportionate for a) smaller wholesale companies and b) small retailers.

We believe that there could be a disproportionate administrative burden on the very small wholesalers on opening of the market, since there is no 'cheap' way of developing systems which can integrate with the market operator. We consider that this should be examined further to understand the likely scale of any problem.

Q34 Do you have any suggestions about the best approach for companies operating wholly or mainly in Wales?

We have no suggestions on the Welsh situation.

Q35 Do you have any comments about the circumstances in which a retail supplier should be able to opt out of Supplier of First Resort ('SoFR') arrangements?

We have no comments on retailer opt out of SoFR arrangements.

Q36 Do you agree with our proposed approach for the developer services market and the related process proposed within MAP3?

The key issue around Developer Services is that the customer (the Developer in this instance) should be provided with an appropriate service by both Retailer and Wholesaler. The market must facilitate this.

There are clearly situations that will occur where a property intended for domestic use is temporarily included in the non-household market. Such situations should be minimised by the market rules and should be easy to rectify through market processes.

Sensible definitions of eligibility will improve this difficult area.

There must also be appropriate mechanisms for charging for usage of water on development sites prior to occupation by either an HH or an NHH customer. There is a strong case for a universal approach to this, which also encourages notification of occupier details by the developer to the market or the HH retailer.

Q37 Do you agree with our assessment of the interactions between the various parties?

Figure 6 provides a clear indication of the potential interactions in the developer services market and how we expect this area to evolve. There are some challenges as to how this will operate effectively where there is a WoC and a WaSC in place.

Q38 Do you agree with principle that Special Agreements should be contestable and the current thinking on the details of the approach outlined in section 9.2.5?

We believe that the concept of special agreements being contestable within the market is reasonable, however many complex special agreements may be difficult to administer within the constraints of the market operator's systems.

Q39 Do you agree with the principle that there should be early publication of wholesale charges and the current thinking on the details of the approach outlined in section 9.3?

Early publication is a reasonable principle, we suggest October makes more sense than July, giving the wholesaler half a year to publish and the retailer the same time

to react. Price Reviews should be timed to make sure these timings can still be realistically delivered.

Q40 Do you agree that wholesalers should only levy charges that are in their wholesale charges schemes or published as special agreements? If not, please provide arguments as appropriate to support your position.

Yes, although only applies to regulated charges.

Q41 Do you agree with our proposed approach to implement these licence changes? If not, how should we go about making these changes?

We agree with the proposed approach.

Yours faithfully,

Tim Orange,
Finance, Regulation and Business Services Director,
South Staffordshire Water PLC