



## Water Services Regulation Authority

### Water Industry Act 1991 Sections 8 and 13

**Notice of proposals by the Water Services Regulation Authority (Ofwat) that South Staffordshire Water PLC (South Staffordshire) replace Cambridge Water PLC (Cambridge) as the water undertaker for Cambridge's water supply area and for the consequential modification of South Staffordshire's conditions of appointment.**

#### The process

This notice begins a period of public consultation. Any representations or objections about any of the matters described below should be in writing (including e-mail) and sent to:

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Any representations or objections must be received by **5.00pm on 21 February 2013**.

#### The Proposal

**That South Staffordshire replaces Cambridge as water undertaker for Cambridge's area**

South Staffordshire and Cambridge each hold an Appointment from the Secretary of State as a water undertaker. Since the merger between South Staffordshire and

Cambridge (which the Competition Commission subsequently approved), both water undertakers are subsidiaries of Alinda Capital Partners LLC.

In brief, South Staffordshire considers the benefits to unify the operations of South Staffordshire and Cambridge are to:

- i) improve the resilience of operations and customer service in the Cambridge area; and
- ii) reduce the corporate costs of operating two separate companies.

South Staffordshire also confirms the following commitments made to the Competition Commission during the [merger enquiry](#) (which resulted in the approved merger) in May 2012.

- i) The current level of customer service will be maintained.
- ii) Separate charging levels in the two areas to be maintained.
- iii) The Cambridge Water name will be retained.
- iv) Local operational staff, including call centre and administration, together with senior management will be retained in Cambridge.
- v) Any corporate costs saved from the synergies of operating as one company will benefit customers from the start of the next price review in 2015. The form of this benefit to customers will need to be decided in conjunction with the existing local customer engagement groups.
- vi) A non-executive director with links to the Cambridge area will be appointed to the Board of the unified company.

The companies are under common control. We therefore consider that the proposed unification of the two companies under a single licence has little impact on Ofwat's ability to make comparisons between regulated water companies.

We propose that South Staffordshire's Appointment as a water undertaker should be varied, so that it also applies to the area currently served by Cambridge. If that happens, Cambridge's appointment will be terminated. South Staffordshire and Cambridge have agreed these proposals. We would encourage representations to be made on our proposals by all interested parties.

We will take into consideration any representations or objections as part of this consultation prior to determining whether we will make the variation to South Staffordshire's licence.

## **Proposed modification of South Staffordshire's Conditions of Appointment as a water undertaker**

### **Price limits and charges to customers**

On 26 November 2009 Ofwat determined new price limits (often called K factors) for both South Staffordshire and Cambridge for the five years beginning 1 April 2010. If this proposal goes ahead, South Staffordshire's price limits will be modified to represent the combined price limit for the enlarged area for 2013-14 and 2014-15.

The K factors for each of the companies will be combined into a single price limit for the respective year effective from 1 April 2013. The average increase in a basket of charges for South Staffordshire (including those for Cambridge) for any year must not exceed that year's combined single price limit.

Each licence-holder must ensure that its charges do not unduly discriminate against or give undue preference to, particular classes of its customers. However, the areas currently served by South Staffordshire and Cambridge are operationally different and their current price limits and amounts charged to customers differ. To provide assurance to customers in the Cambridge region, we propose to include wording in Condition E of South Staffordshire's conditions of appointment which provides that until 31 March 2015, customers in Cambridge's area will not have higher charges than they would have done if Cambridge's licence had not been terminated. In order to monitor this, we propose to include wording in Condition E to require separate Principal Statement information to be provided for each of the separate areas until 31 March 2015.

As a consequence of this transitional provision, and to provide reassurance to South Staffordshire, we also propose to include wording in Condition E to provide that differences in tariffs in each area until 31 March 2015 will not breach its obligation to ensure that its charges do not unduly discriminate against or give undue preference to, particular classes of its customers.

There will still be a requirement under Condition E to ensure that undue preference and discrimination is avoided as between classes of customers within each of South Staffordshire and Cambridge's water supply areas.

After 31 March 2015, South Staffordshire will still be required to ensure that undue preference and discrimination is avoided as between the current South Staffordshire and Cambridge water supply areas.

## Ring fencing provisions

South Staffordshire accepted the latest suite of ring fencing licence conditions in 2008 following its change of ownership. Amongst other things, these conditions:

- require South Staffordshire to act at all times in the manner best calculated to ensure that it has adequate systems of planning and internal control to enable it to secure the carrying out of its regulated activities. This also requires South Staffordshire to submit an annual certificate that, in the opinion of the Directors, South Staffordshire will, for at least the following 12 months, have adequate systems of planning and internal control which are sufficient to enable it to carry out its functions:
- require South Staffordshire to maintain a listing of a financial instrument whose market price should reflect the financial position of South Staffordshire. Although not a substitute for an equity listing, this would ensure the existence of a helpful financial comparator;
- require South Staffordshire to use all reasonable endeavours to maintain an investment grade credit rating for its corporate debt; and
- include the cash lock-up provisions which would prohibit, subject to certain limited exceptions, and without Ofwat's prior consent, the transfer of cash or other assets to an associated company in certain circumstances where the company's investment grade rating is threatened.

We do not propose any modification to South Staffordshire's ring fencing provisions in Condition F of South Staffordshire's conditions of appointment, but invite views whether any modifications should be made.

## Service and Performance information

The water supply areas currently served by the two companies are geographically and operationally separate. So we can monitor whether South Staffordshire has met the outputs required by both companies' 2009 price limits, Ofwat proposes to modify conditions J and M of South Staffordshire's conditions of appointment, so that South Staffordshire will continue to hold separate information for this purpose. Thereafter, South Staffordshire may be required to collect and maintain separate data on matters such as supply and demand issues due to the difference in the water resources positions in each region.

## **Fees**

To avoid any doubt as to how the fees to be paid to Ofwat are calculated, we propose inserting a paragraph into Condition N of South Staffordshire's conditions of appointment stating that the turnover for any period prior to the unification of the two licences in relation to which future fees are set should be the combined turnover of South Staffordshire and Cambridge.

## **Codes of practice and plans**

We propose to modify Conditions G, H, I and L of South Staffordshire's conditions of appointment to provide that Codes of practice and plans can be submitted as one code of practice or plan; or two separate codes of practice or plans for the current South Staffordshire and Cambridge areas. We propose to require that where one code or plan is provided separate provision is made for the two areas within the code or plan.

## **Other**

We propose to take this opportunity to update or delete any outdated terms and references throughout South Staffordshire's conditions of appointment. For example, references to Companies Act 1985 will now be to Companies Act 2006 and references to the 'Director' will now state the Water Services Regulatory Authority.