



## **Granting consent under Condition R to enable Sembcorp Bournemouth Water to sell water to Avon Valley Water**

### **1. Introduction**

On 24 April 2013, Sembcorp Bournemouth Water Limited (Sembcorp Bournemouth Water) asked the Water Services Regulation Authority (Ofwat) for consent to sell water to Avon Valley Water Limited, a related licensed water supplier.

Paragraph 5(1) of Condition R of Sembcorp Bournemouth Water's appointment as a water undertaker (licence) states that it cannot sell water to a related licensed water supplier without our consent:

**“If and for so long as the Appointee is related to any licensed water supplier -**

**(a) it shall not without the consent of the Authority sell (or otherwise make available) to that licensed water supplier any water, or any of its other assets [...].”**

On 14 January 2014, Ofwat granted consent for Sembcorp Bournemouth Water to sell water to Avon Valley Water.

This notice gives our reasons for granting consent.

### **2. Sembcorp Bournemouth Water's proposal**

Sembcorp Bournemouth Water provides a supply of non-potable water to a large industrial customer (Esso) in Southern Water's area, and has done so since 1955. Esso uses most of this supply itself, but has traditionally sold on a small amount to a number of large industrial users (“tenant customers”) on its own private network.

Esso wanted to stop this water resale arrangement to its tenant customers and, after inviting and considering bids from other companies, it selected Avon Valley Water to supply water to the tenant customers.

### **3. Our duties**

In assessing this request, we considered our relevant duties, including those under section 2 of the Water Industry Act 1991 (WIA91). In particular, we considered our duties to:

- further the consumer objective (section 2(2A)(a) of WIA91) to protect the interests of consumers, wherever appropriate by promoting effective competition;
- secure that companies holding appointments as water and sewerage undertakers are able to finance the proper carrying out of their functions (section 2(2A)(c) of WIA91); and
- (a secondary duty) ensure that consumers are protected as respects any activities of any person appearing to Ofwat to be connected with such companies and that any transactions are carried out at arm's length (section 2(3)(d) of WIA91).

### **4. Further considerations**

In considering the application from Sembcorp Bournemouth Water, Ofwat considered whether there were risks to competition, particularly bearing in mind the planned opening of the non-household retail market in 2017.

#### **4.1 Market foreclosure**

When the Water Bill is enacted, we expect the non-household retail market to open in 2017, at which point each of the tenant customers on Esso's private network will potentially be able to choose its water supplier. If Avon Valley Water were to agree long term contracts with the tenant customers in advance of market opening, then they would be locked in with Avon Valley Water. This would effectively close off the tenant customers to future competition for the period of any such contract and the potential benefits of market opening would therefore be lost.

In response to this concern Avon Valley Water has confirmed to us in writing that it will not sign contracts longer than four years with the tenant customers, which mitigates any risk of foreclosure of this market due to the length of contract.

#### **4.2 Barriers to entry**

A retailer would need access to Esso's private network to service the market. If Avon Valley Water, due to the legacy of the special agreement between Sembcorp Bournemouth Water and Esso, has any advantage to access the private network,

then this is a potential barrier to entry for other retail licensees to compete in the market.

However, any potential risk to competition as a consequence of the legacy agreement has to be weighed against the requirements of the customer. Esso has made a business decision to withdraw from the activity of water resale to the tenant customers on the site. It would not be appropriate for us to impose requirements on an unregulated reseller to require it to continue in a course of business that is against its business plan nor to interfere in its freedom to contract in the interests of its core business.

We therefore consider that it is for Esso to negotiate access to its network. Its ability to do so is an important factor within the overall consideration of the acceptability of the application from Sembcorp Bournemouth Water.

#### 4.3 Customer choice

We take customer choice seriously, and in this case Esso has said it would like:

- to cease being a water reseller; and
- Avon Valley Water to supply water to the tenant customers.

#### 4.4 Arm's length transactions

Any consent under Condition R for Sembcorp Bournemouth Water to sell water to Avon Valley Water is without prejudice to the other legal requirements that apply to Sembcorp Bournemouth Water. In particular, Sembcorp Bournemouth Water will still be required to ensure that every transaction with an associated company “**is at arm's length, so that neither gives to nor receives from the other any cross-subsidy**” (paragraph 6 of Condition F of Sembcorp Bournemouth Water's licence).

The customers of Sembcorp Bournemouth Water will therefore be protected in relation to the activities of Avon Valley Water i.e. the transaction will not be to the detriment of those customers, and there should not be any effect on the ability of Sembcorp Bournemouth Water to finance its functions as a water undertaker.

### 5. Conclusion

Having assessed Sembcorp Bournemouth Water's request, we decided that it was appropriate to grant consent for the reasons set out above.