



# Ofwat's consultation on the review of non-household retail price controls

## 1. Introduction

- 1.1 The Consumer Council for Water (CCWater) is the statutory consumer organisation representing water and sewerage customers in England and Wales. CCWater has four regional committees in England and a committee for Wales.
- 1.2 We welcome the opportunity to respond to Ofwat's consultation on its proposed approach to reviewing the non-household retail price controls set for incumbent regulated water and sewerage companies, as confirmed in the 2014 final determinations.

## 2. Executive Summary

- 2.1 During the 2014 price review process, CCWater consistently stated that the introduction of default tariffs based on the new non-household retail price controls should not lead to disproportionate or sudden tariff increases for any groups of non-household customers. This is because there is a risk of a negative reaction from non-household customers if they see a bill increase due to a change in the design of their tariff, or apparently as a result of competition.
- 2.2 In this context, we support Ofwat's review of the non-household retail price controls in 2016 because we recognise that when the price controls were set in 2014 there was some uncertainty over the companies' allocations of costs between wholesale and retail (and between household and non-household retail within the retail price controls).
- 2.3 We also agree that the review should be restricted to the allocation of both costs and the net margin within the price controls because there is no fresh evidence to justify a review of the net margin itself or the efficiency challenges incorporated into the 2014 price controls.
- 2.5 We support the principle of achieving more consistency in default tariff structures, but companies need to ensure that any changes to customers' existing tariffs are introduced gradually and are communicated well to customers. Revised tariff structures should also be consistent with competition law.
- 2.6 We also support the intention for companies to engage with CCWater, Customer Challenge Groups and, possibly, customers directly if this review leads to significant changes in default tariffs.

## 3. Responses to consultation questions

### Q1 Should this review focus only on issues relating to the non-household retail price controls and the default tariff price caps?

- 3.1 Yes. Ofwat's 2014 final determinations confirmed its intention to review only the non-household price controls and default tariff caps in 2016. Re-opening other aspects of the final determinations would create uncertainty for customers' bills, and potentially undermine the work CCWater, Customer Challenge Groups (CCGs) and others contributed to the 2014 Price Review to ensure it delivered an outcome that reflects evidence of customers' views and is acceptable to customers.

- 3.2 The review of the non-household price controls in 2016 is justified as, at the time of Ofwat's 2014 final determinations, there was uncertainty over some of the cost allocations used to set these price controls. This was mainly due to the on-going process to reallocate costs due to the separation of retail and wholesale functions in regulated businesses. As it is important that the backstop protection provided by default tariffs reflects accurate costs, we welcomed the intention to review this aspect of the 2014 price settlement in time for retail market opening in April 2017.
- 3.3 Ofwat should help ensure that any subsequent changes to default tariffs in 2016 are managed in a way that minimises any potential negative impacts to customers. Companies should identify the customers who may be affected (particularly negatively), with changes introduced gradually with written communication with customers to explain the changes made. This will also be an opportunity to advise customers of the availability of a choice of retailer from April 2017.

**Q2: In considering non-household retail issues, should this review allow for the reallocation of costs and margins between default price caps, but with the constraint that aggregate levels of non-household retail costs and margins remain the same as in the existing controls, consistent with the expectations set out in our final determinations?**

- 3.4 Yes. Our expectation was that the review of non-household price controls would be related to new and/or improved information that companies can provide about costs relating to the provision of non-household retail services, and how they are allocated to default tariffs. However, we would reiterate in Paragraph 3.3 above about transition and communication.
- 3.5 We agree with Ofwat that there is no new information to justify a review of the 2.5% non-household retail net margin, or the efficiency challenges incorporated into the 2014 price controls. We have previously raised concerns that the introduction of default tariffs, especially before market opening, raised the risk of some non-household customers seeing a bill increase because of a 're-design' of tariffs to comply with this price control. Restricting the review of the price controls to new or revised cost information may help mitigate this risk, if the revised cost and margin allocations lead to any changes in customers' existing tariffs.

**Q3: How can transparency in the mapping of tariff caps to default tariffs be improved?**

- 3.6 Non-household customers could be informed that the default tariff applied to their bill is designed as a 'backstop' price protection and that once the market opens, they can either switch to an alternative tariff offered by another retailer or negotiate an alternative tariff with their existing retailer.
- 3.7 This could be achieved by:
- Publishing information in billing literature and company websites to explain to customers what the default tariff is and how it differs from customers' previous tariffs (where applicable). This should be accompanied by advice that customers have the option to either consider alternative retailers' offerings or contact their existing retailer for information about other tariff options that may be available.

- Presenting information for customers on default tariffs in a clear and simplified way, not only to help ensure they are understandable, but to help customers make easier comparisons with alternative tariffs on offer. We would like to work with Ofwat on developing guidelines for incumbent companies to use in providing this information.

3.8 We would also like to see Ofwat provide guidelines to companies on managing the transition from old to new default tariff structures, where a company significantly changes existing tariffs as a result of this review. This could identify whether further engagement with non-household customers is required to:

- gather views or measure the likely customer reaction to any new tariff structures; or
- address any issues that may arise if a company's customer information about its revised default tariff structure is not clear or easily understood.

**Q4: Do you consider it appropriate to encourage companies to increase the consistency in default tariff structures and consider carefully whether the diversity in the present levels of default tariffs is properly justified?**

3.9 Yes, in principle if this helps to reduce potential customer confusion over the range of tariffs available. However, introducing greater consistency has a risk of creating 'winners and losers', as there may be some customers who could see a bill increase because the design of their existing default tariff is made consistent with that of other retailers.

3.10 To address this risk, companies should identify the customers who will see changes to their existing tariffs and manage this transition in a way that mitigates any negative impact. Companies should engage with Ofwat and CCWater to set out the options for:

- streamlining tariffs to generate more consistency; and
- mitigating the impact of significant bill increases that a more streamlined structure may produce.

CCWater and Ofwat can both advise how best to progress the issue. Companies may also wish to engage further with customers directly on such options to inform such a decision.

**Q5: What information should companies be asked to provide and publish in support of any proposals (including for no change) in respect of their default tariff caps?**

3.11 We agree with Ofwat's suggestion in the consultation paper that information should be provided on:

- the allocation of costs and margins;
- any evidence of customer views of the default tariff structure a company has introduced; and
- assurance of how the tariff structure complies with competition law.

As well as providing transparency for customers, this will also be beneficial for the required level playing field for retail market participants.

3.12 Furthermore, companies should also provide Information about the number of customers who will see a change in their existing tariffs, and how these changes will be introduced and communicated.

**Q6: Do you consider it appropriate to allow companies not to update their cost and margin attributions and allocations and so retain their existing default tariff price caps?**

3.13 Yes, but only if a company can demonstrate that no new information has emerged that implies a change is required, and that the existing default tariff structure complies with competition law and has evidence of approval by CCWater and Ofwat.

**Q7: Is a three year duration appropriate for the next non-household price control and if not what is the most appropriate direction and why?**

3.14 Yes, as this aligns with existing household retail and wholesale price controls, and allows time for Ofwat to see how retail competition develops. The 2019 price review provides an opportunity to deal with any further issues or fresh information on cost and margin allocations that emerge in the intervening years.

**Q8: Do you agree with the proposed timetable for this review with a statement of method in April 2016, draft determinations in September 2016 and final determinations in December 2016?**

3.12 Yes, as this allows sufficient time for appropriate consultation with CCWater and others between each stage of the process.

## Enquiries

Enquiries about this consultation response and requests for further information should be addressed to:

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