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Guidance on compliance codes

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Purpose of this document

This document provides guidance to water companies on the key issues that need to be covered in their compliance codes, but is not intended to cover all eventualities. It will be reviewed and updated in the light of experience. It is not, however, a substitute for condition R and should be read alongside that condition.

Paragraph 7(4)(a) of condition R requires water companies to have in place a compliance code which adheres to our compliance guidance. Water companies need to make arrangements (details of which should be contained in their compliance codes) to:

- ensure that they are complying with the confidentiality obligations under appointment condition R;
- protect commercially sensitive information received from or in relation to licensed water suppliers (licensees);
- ensure that transactions between themselves and any associate licensee are at arm's length;
- provide clear information to staff on their individual obligations; and
- ensure that they are carrying out their functions under the water supply licensing (WSL) regime fairly and without discriminating against customers or licensees.

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1. Introduction

1.1 Background to appointment condition R

Condition R supports the duties placed on water companies by sections 66A-66C of WIA91 with regard to providing access to licensees on reasonable terms.

Condition R ensures that each water undertaker:

- produces, publishes and updates as necessary a code for access (including prices) in compliance with the access codes guidance;
- does not unfairly discriminate between licensees (or their customers) and their other customers;
- does not obtain an unfair commercial advantage because of their activities under this condition (this also applies to any associates of a water company); and
- produces, publishes and updates a compliance code which follows our guidance.

Condition R also requires that water companies do not show undue preference to, or undue discrimination against, actual or potential customers or any licensees. This will prevent unwarranted distinctions between:

- a water company's retail activities and licensees;
- different licensees (or their customers); or
- customers connected to the water company's network, whether or not they are supplied by a licensee or the water company. A water company should not treat a licensee's customer any differently from its own customers (unless specifically agreed as part of an access agreement). For example, if there is a drought order or a hosepipe ban, the water company cannot require the licensee's customers to limit their water use in precedence or preference to limiting water use by its own customers.

2. Obligations under appointment condition R

This chapter outlines the duties on water companies under condition R which fall within the scope of this document. It also provides guidance on the key issues that each water company should cover in its compliance code, including the types of procedures to prevent any breach of its obligations under this condition. The points set out in this chapter are intended to be examples and form a non-exhaustive list.

Paragraph 7(4) of condition R defines compliance guidance as guidance in relation to a water company's compliance with its obligations under paragraph 7 (obligations about information) and 5(1)(b) (arm's length trading) of this condition; and generally in relation to any obligation of confidentiality on a water company in relation to information provided to or by it under or for the purposes of this condition or condition S (customer transfer protocol), and its compliance with those obligations.

In addition, paragraph 7(4)(c) of condition R requires each water company to review its compliance code once a year (by no later than the anniversary of the date that we first issued compliance guidance). Water companies can revise their compliance codes at any time and should do so whenever we issue any revised guidance (after we have consulted on this). They should follow our timetables when doing this.

2.1 Arm's length trading

Under paragraph 5(1)(b) of appointment condition R, a water company that is related to a licensee must ensure that transactions between the two are carried out at arm's length, that is as though the parties are unrelated.

A related licensee may call on the skills and experience of staff and other resources of the water company only where the service provided by those staff or use of those resources is properly charged and accounted for. This may include, for example, the use of staff employed by the regulated business (including during the application stages of the licensing process) or buildings, equipment and other resources.

We do not stop any individual from being a director of both a water company and a related licensee. We do, however, consider that directors must be aware of their company's duties under condition R. For example, if a director receives information when negotiating an access agreement in their capacity as director of a licensee, they should not use it in their capacity as director of a water company, unless this is allowed for in standard licence condition 2.

We would carefully consider a licence application which proposed a Board made up of persons holding posts within the water company. Such consideration could, for example, include requiring the applicant to provide details of its compliance procedure, including its compliance code.

Water companies' compliance codes should include details of any related licensees and should clearly set out the procedures staff are required to follow when handling transactions and details of how staff should account and charge for services provided to a related licensee. It may be helpful for water companies to include a standard set of procedures applying to all licensees within their compliance codes to reduce the risk of discrimination against individual licensees.

Any service to a licensee should be clearly noted in the financial records of the licensee and the water company and comply with Regulatory Accounting Guideline 5 (RAG5), licensees' standard licence condition 7 (area of operation and arm's length transactions) and paragraph 5 of condition R (anti-competitive behaviour).

Water companies should read paragraph 6 of Condition F of their appointment (Transactions entered into by the Appointee or the Appointed Business with or for the benefit of Associated Companies or other businesses or activities of the Appointee) before developing their policies and procedures in relation to arm's length trading and including this information in their compliance codes.

2.2 Obligations about information

Each water company must ensure that neither it, nor any related company, obtains any unfair commercial advantage from any exchange of information specified under paragraph 7 of condition R. For example, a water company may have access to confidential information about a licensee's activities which it might be able to use to gain an unfair commercial advantage.

In the course of providing access under sections 66A-66C of WIA91, water companies will need to obtain information from licensees. This may include details of:

- customers supplied by the licensee;
- its water sources;
- water quality; volume and timing of water to be supplied;
- the security of supply associated with the licensees' water sources; and
- meter reading details.

Under paragraph 9 of condition R, a water company cannot request from a licensee or from a person supplied or seeking to be supplied by a licensee more information than it reasonably requires:

- to carry out its functions;
- to ascertain whether the licensee has sufficient product and public liability insurance;
- to comply with any condition of its appointment;
- in relation to national security or civil emergencies; or
- to comply with any reasonable request for information made by the Environment Agency.

Water companies may only use the information a licensee provides (or that relates to a licensee) in relation to the WSL regime for the purpose for which it was supplied. Each water company must also take appropriate steps to protect any information it receives from misuse within the company itself. The purpose of paragraph 7 of condition R is not only to prevent inappropriate disclosure of information to third parties (such as those outside the water company) but also within the water company (such as to other employees or agents of the water company itself). Licensees and water companies must agree a pre-contract confidentiality agreement at the start of their negotiations (paragraph 7(1) of condition R). This is so that both parties can be sure that neither may misuse nor disclose without consent information received as part of the access negotiation process.

Compliance codes should set out how such information received from or in relation to licensees will be handled and provide details of the person or team responsible for this information. It is essential that information a water company receives from or relating to a licensee is not misused or used to gain an unfair commercial advantage. Compliance codes should therefore set out the procedures in place to prevent this.

In addition, compliance codes should set out procedures for sending information to licensees. For example, under paragraph 8 of condition R, a water company should provide a licensee with the information the licensee reasonably requires to:

- enable the licensee to apply for, negotiate and conclude an agreement under section 66D WIA91;
- comply with any condition of its water supply licence, or any statutory requirement imposed in consequence of its water supply licence; or
- comply with any reasonable request for information made by the Environment Agency.

Water companies may decide to ensure that all dealings with licensees are handled separately from those with customers. This would reduce the possibility of information being used inappropriately and remove any perception that a water company could be trying to persuade a customer not to switch supplier. Examples of the steps taken by some water companies to protect information received from or in relation to a licensee include:

- assigning different team members to deal with requests from licensees and customers;
- changing security settings on confidential computer folders;
- using separate rooms to discuss licensee issues and customer issues;
- having different e-mail addresses to handle correspondence from customers and licensees separately; and
- using a different building to any related licensee.

It may be helpful for water companies to set out some examples of situations that are relevant to compliance with condition R in their compliance codes and provide guidance to staff on how to deal with these. This should make relevant employees aware of what constitutes a breach.

Where we are satisfied that information is being, or is likely to be, misused in breach of condition R, we can use our enforcement powers to secure compliance. Since April 2005 we have had the power to impose financial penalties of up to 10% of turnover where a company contravenes its appointment conditions.

3. General areas

Water companies' compliance codes should provide enough information to demonstrate that they are complying with the relevant obligations under condition R. The aim of a compliance code is to help maintain a culture of compliance within a company.

3.1 Staff training

Compliance codes should include details of the training available to staff in relation to the areas of compliance highlighted in chapter 2. Awareness of the compliance code among all relevant employees is necessary if it is to be effective. Training will be an important part of an effective compliance code and is essential for all employees who deal with licensees and customers. The type of training should be tailored to each water company's particular requirements, but could, for example, be offered as part of the induction programme for new staff and at regular intervals to update staff with any changes.

3.2 Compliance statement

We expect each water company's compliance code to include a clear statement of their approach to compliance. This could be a personal message to staff from the most senior person in the organisation, stating their commitment to the compliance code or a general statement made on behalf of the organisation, including evidence of how this message is repeated throughout the company. This statement should also make clear to the water company's employees why compliance with the obligations under condition R is important.

3.3 Monitoring or audit process

Evaluating the compliance code regularly will be essential not only to ensure the code is working properly but also to enable areas of risk to be identified and addressed. Details of the process for monitoring the effectiveness of the compliance code should be included in the compliance code itself. Evaluating the code could include the following elements:

- testing individual employees' knowledge of the code, including policy and procedures; or
- audits to check for actual or potential breaches of the code.

3.4 Disciplinary process

Each water company's compliance code should include details of the disciplinary procedures in place for breaches of condition R. This will be essential in making the relevant employees aware of the consequences of a breach of this condition.



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