



**Review of retail household markets
in the water and wastewater sector
- an Ofwat call for evidence**

submission two - answers to questions

1 Introduction

The Consumer Council for Water (CCWater) is the statutory consumer organisation representing the interests of customers of water and sewerage companies in England and Wales. CCWater has four regional committees in England and a committee for Wales.

We welcome the opportunity to respond to Ofwat's call for evidence relating to its '*Review of retail household markets in the water and wastewater sector*'.

On 11 February 2016, we submitted to Ofwat a summary of the historical and upcoming research we have conducted of customers and their representative groups relating to retail markets. One of our upcoming research projects specifically asks household customers about their attitudes to competition. We will share this evidence when it is available in May 2016.

This second submission aims to answer the four questions Ofwat asks in its call for evidence. CCWater is currently undertaking a desk research project to look at lessons learned in other competitive household markets which will be available by April 2016. This project will help us build on our answers below and we will share the findings with Ofwat when they are available.

2 Response to Ofwat's questions

Q1. What are the advantages and disadvantages of extending competition to retail services in the water and sewerage sector to household customers? How could this best be achieved?

Extending competition to the household market provides potential advantages to customers:

- Empowerment of customers by allowing them to “vote with their feet” and switch retailer. We expect some customers will be motivated to switch if:
 - Another retailer can offer a better price or more specialised tariff;
 - Another retailer can offer a better or more specialised service (e.g. combined bill with energy or telecoms, or both); or
 - Their current retailer has provided a service that the customer considers to be below standard;
- Better customer information as incumbent companies or new retailers strive to correct account errors or help customers find the best tariff; and
- Pressure on companies to offer a good price and service or risk losing customers to competing retailers.

However, there are potential disadvantages:

- Some customers could experience poor practices that did not exist before:
 - A “hard sell” where customers are encouraged by retailers or third party intermediaries to switch when they may not want to;
 - Mis-selling, where customers do not get what they were promised after switching;
 - Too many, or overly complicated tariffs which could make it difficult for customers to compare between offers or retailers;
 - Retailers cherry-picking the most profitable customers while ignoring those with higher costs to serve;
 - Resolution of and communication about operational problems may be more difficult with retailers involved; and
 - If the household retail market undermines investor confidence this could lead to an increasing cost of capital and higher customer bills.
- Industry stakeholders would have to re-evaluate how existing safety nets for financially vulnerable customers would be managed:
 - How would retailers support customers with long term debt management problems?
 - Would indebted customers be prevented from switching?
 - Will retailers fund or administer social tariffs?
- A competitive household retail market may not live up to customer expectations:
 - Our joint research with Ofwat in 2008 showed that price was the main reason customers would switch. If the relatively small retail percentage of the value chain puts new retailers off from entering the market or offering significant price discounts, this could lead in turn to lower customer interest;
 - Some customers may incorrectly assume they are switching their wholesaler in an attempt to resolve issues relating to their water supply; therefore
 - The scope of what services can be switched needs to be made clear to customers.

Metered or unmeasured

Would competition be available to all household customers or only those that are metered? The competitive non-household markets in England and Scotland have been developed to work best when customers are metered. Yet, by 2020, over a third of household customers could still be unmeasured. This poses problems:

- A market that only allowed metered customers to participate might encourage higher customer uptake of meters, but also cause backlash amongst some customers that remain unmeasured, do not want meters or cannot be metered; and
- If the market allowed all customers to participate, how would retailers treat unmeasured customers? Would these customers experience resistance from some retailers that did not want to take them on?

Q2. What scenarios for retail competition could be considered in Ofwat's analysis? What are the advantages and disadvantages of each for water and wastewater services for customers, the environment, wider society and investors?

Eligibility based on different customer segments

Household retail competition could be extended only to customers that fall within, or outside, other segments, For example:

- High or low cost to serve customers;
- Customers who reside within certain geographical areas;
- Customers in “bill on behalf” relationships (e.g. housing association tenants);
- Customers who specifically register their interest in competition (e.g. through a price comparison website, special interest charity, etc.);
- Customers who purchase their water from a reseller (i.e. water resale); and
- Customers of current New Appointments and Variations (NAVs).

Fundamental model

The household market could be modelled after the non-household model where customers choose to switch. Ofwat could consider an alternative “competition for the market” model, albeit one without customer choice, where retailers compete for limited term licences to serve customers or segments of customers.

Winners and losers

It will be crucial that all scenarios set out at what point the benefits of household competition exceed the cost of its introduction for all customers or those in different segments.

As we have seen through compulsory metering programmes or the introduction of new tariffs, any change to the basis of charging creates winners and losers. It is important that the scale and type of customers who will lose out are identified, and that mitigating and transitional arrangements are put in place to reduce the financial impact felt by these customers.

For example, retailers may use introductory offers to attract new customers. If existing customers feel they are subsidising cheaper deals for new customers, this could lead to them feeling like they are unprotected against unfair charges.

Q3. With respect to potential competition scenarios used to support the analysis, what additional risks or opportunities should be captured in Ofwat's analysis? How should these be assessed? What would be necessary for each of the scenarios to be implemented successfully? Over what time period could implementation take place?

Potential risks

Introducing a retailer between the customer and wholesaler may lead some customers to be concerned that communication might be less forthcoming and it might be harder to resolve complaints, particularly about operational issues like supply interruptions or sewer flooding.

There are risks of negative customer perception of a retail market if competition is not offered universally and some customers are left without a choice. It might be complicated and confusing for customers and retailers to operate in a market where only some customers are eligible. Furthermore, if a lesser range of retail services can be switched than in the non-household markets, some customers could perceive this as a reduction in their service level.

If the household retail market undermines investor confidence this could lead to an increasing cost of capital and higher customer bills.

Vulnerable customers

Scenarios need to account for protection of vulnerable customers, particularly what happens to:

- Customers who are “expensive” to serve (e.g. retailers having to read remote meters);
- Customers with poor debt histories;
- Bad debt - who carries it?
- Social tariffs - how will they be funded and administered; and
- Extra care services - can they be protected or will they reduce in scope and scale?

Potential opportunities

Though issues relating to scalability need to be addressed, it is feasible that many of the market codes and IT systems that are being developed for the non-household market could be used for the household market. Therefore, it is possible that market infrastructure could be assembled more quickly and/or at lower cost than it was for the non-household market.

Benefit realisation

Ofwat should consider in its analysis what tangible benefits customers will realise in the shorter term versus the longer term.

Our joint research with Ofwat in 2008 revealed that customer interest in switching was driven primarily by a belief that it would reduce price. The analysis of household competition should show what benefits customers will experience in the short to medium term against these expectations.

Q4. What are the interactions between household water retail and other markets in the water sector and beyond?

Water sector

There are a range of interactions within the water industry that could potentially lead to lower costs to household customers, which in turn could encourage greater participation in the market by some customers. These interactions could include:

- Retailers applying what they learn about water efficiency in the non-household market to household customers;
- Wholesalers becoming more efficient upstream (and passing those cost savings to retailers and eventually customers through lower bills);
- Water trading; and
- Abstraction reform.

Energy sector

Some household customers could be enticed to switch to a retailer that can offer a combined water and energy bill. Therefore, we might see crossover with the energy market or energy providers looking to take on retail water services.

Financial services

Incumbent water companies have built links to financial support networks for vulnerable customers (e.g. Money Advice, Step Change,). We think that some customers would expect this same level of support from the new retailers.

Retailers may introduce novel payment methods to customers (e.g. by mobile phone app, text).

3 Enquiries

If you have any questions about CCWater's response to this call for evidence, please contact:

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