
Proposal by the Water Services Regulation Authority (Ofwat) to vary the appointments of SSE Water Limited (“SSE Water”) and Thames Water Utilities Limited (“TMS”) as water and sewerage companies.

Water Industry Act 1991 Section 8(3)

This notice is a consultation on this proposal. The consultation period will last for 28 calendar days. Having considered any representations submitted in response to the consultation, Ofwat will decide whether or not to make the variations to these companies' appointments.

The Site

On 16 March 2016, SSE Water applied for a variation to its appointment to provide water and sewerage services to a new residential development in Nine Elms, London. The development, called Embassy Gardens Phase 2 (the Site), will consist of 872 new residential properties and is, at present, in TMS' water supply area and sewerage services area. It is adjacent to a site that has been served by SSE Water for water and sewerage services since September 2013 called Embassy Gardens. SSE Water expects the Site to be fully developed by 2019.

The proposal

Ofwat proposes to:

- vary the appointment of SSE Water as a water and sewerage company by adding the Site to its water supply area and its sewerage services area; and
- vary the appointment of TMS as a water and sewerage company by excluding the Site from its water supply area and its sewerage services area.

By means of these variations, SSE Water will become the water and sewerage services supplier for the Site.

Policy for new appointments and variations

The new appointment and variation mechanism, set out in primary legislation¹, provides an opportunity for entry and expansion into the water and sewerage sectors by allowing one company to replace the existing appointee as the provider of water and / or sewerage services for a specific area. This mechanism can be used by new companies to enter the market and by existing appointees to expand their businesses.

When considering applications for new appointments and variations, Ofwat operates within the statutory framework set out by Parliament, including our statutory duty to protect consumers, wherever appropriate by promoting effective competition. In particular, in relation to unserved sites, we consider that we must ensure that the future customers on a site – who do not have a choice of supplier – are adequately protected. When assessing applications for new appointments and variations, the two key policy principles we apply are that:

- customers, or future customers, should be no worse off than if the site had been supplied by the existing appointee; and
- Ofwat must be satisfied that an applicant will be able to finance the proper carrying out of its functions as a water and/or sewerage company.

We clarified these two policy principles in February 2011 when we published our 'New appointments and variations – a statement on our [policy](#) and [process](#) for new appointments and variations'. In November 2012, we published '[Statement on our approach for assessing financial viability of applications for new appointments and variations](#)'. This states that we will adopt a company-based assessment of financial viability, rather than a detailed site-based assessment, where it is appropriate to do so.

When we assess whether customers will be no worse off as a result of the appointment, we not only consider the customers on the site but also the generality of customers. These include not only the customers of the existing provider but also

¹ The legal framework for new appointments is set out in the Water Industry Act 1991 (WIA91). Section 7 of the WIA91 sets out the criteria by which an appointment or variation may be made. Section 8 sets out the procedure for making that appointment or variation.

customers more generally across England and Wales, who in our view benefit from the effective operation of the new appointment and variation mechanism.

The application

SSE Water has applied to be the water and sewerage company for the Site under the unserved criterion set out in section 7(4)(b) Water Industry Act 1991.

Unserved status of the Site

To qualify under the unserved criterion, an applicant must show that at the time the appointment is made, none of the premises in the proposed area of appointment is served by the existing appointee.

SSE Water has provided maps showing the water and sewerage boundaries for Embassy Gardens Phase 2 overlaid on the TMS asset maps. There is currently one connected customer who is billed by TMS for water and sewerage services, but SSE Water has explained that the developer plans to disconnect and demolish this customer's premises in July 2016. TMS has agreed that the site will become unserved following this demolition.

Given this information, we are satisfied that provided this demolition takes place, the Site will be unserved at the time of the variation of appointment, if the variation is granted.

Protecting customers

Ofwat acts to protect consumers, especially those who are unable to choose their supplier. In assessing applications to supply new development sites, Ofwat acts on behalf of end-customers who are not yet on site, to protect their interests. The fact that future customers on a site have not directly chosen their supplier is not a

position unique to new appointments – very few customers in England and Wales are able to choose their supplier².

Recognising this, our assessment of an applicant’s proposals includes analysis of its plans to ensure customers will be at least no worse off in terms of their annual bills and levels of service than if they had been supplied by the existing appointee. We will continue to protect customers on the Site by regulating the new appointee's prices and service levels.

Customers on the Site - price

SSE Water intends to purchase a bulk supply of water from TMS to supply the Site and intends entering into a bulk discharge agreement with TMS enabling the Site to discharge into TMS’ sewerage system.

SSE Water proposes to charge customers based on TMS’ existing metered water and sewerage household tariffs. SSE Water is not offering a discount on these tariffs. SSE Water will offer the WaterSure³ tariff to qualifying customers.

Having considered SSE Water’s pricing proposals, we are satisfied that customers will be at least no worse off in terms of their annual bills than if they had been served by TMS.

² The only customers that can normally choose their supplier are non-household customers that consume at least 5MI per year and are supplied by a company that is wholly or mainly in England (and at least 50MI for companies wholly or mainly in Wales) and satisfy the Water Supply Licensing (WSL) eligibility criteria. Those non-household customers that consume at least 50 MI in England (and at least 250 MI in Wales) can switch suppliers under either the WSL regime or under the new appointments regime. This will change in April 2017 in England, in that the 5MI threshold will no longer apply and any non-household customer will be able to choose their supplier.

³The WaterSure scheme allows households on meters who receive certain means tested benefits or tax credits, and who are either responsible for three or more children under the age of 19, or have a medical condition which requires significant additional use of water, to pay no more than the average household bill for its region.

Customers on the Site - levels of service

SSE Water is subject to the same customer service level requirements as other water and sewerage appointees.

Guaranteed Standards of Service (GSS) compliance and base service levels

SSE Water has submitted information about its proposed service levels, under:

- the statutory requirements of the GSS Regulations;
- our service indicators; and
- its own company standards.

We have assessed these planned levels of service and are satisfied that they match or exceed those typically achieved by TMS and the sector as a whole.

Codes of Practice

Every appointee is required under conditions G, H and I of its conditions of appointment to publish debt, leakage and customer Codes of Practice. We have assessed SSE Water's Codes of Practice, and are content that customers on the Site would be no worse off being served by SSE Water rather than by TMS.

SSE Water's voluntary standards

We have also made a detailed check of SSE Water's voluntary service standards, including where it enhances the statutory GSS provisions. We require that SSE Water matches or exceeds TMS' own standards (except where there is reasonable justification for not doing so).

Examples of where SSE Water will match or offer improved customer service compared with TMS include:

- SSE Water offers £35 compensation if a customer regularly receives heavily discoloured water, whereas TMS does not offer compensation in these circumstances;
- SSE Water matches TMS' payment for failing to keep appointments (without giving the customer 24 hours' notice). Both companies offer £50;

- SSE Water also offers several additional standards which TMS does not offer. For example, SSE Water will pay £30 if it fails to read a customer’s meter once per year; £35 if it doesn’t make a refund within 10 days for an overpayment due to company error; and £35 if it refers a debt to a debt collection agent which proves to be unfairly pursued or if the agent acts improperly;
- SSE Water matches TMS’ 10 working day service level for the number of days taken to respond to billing enquiries;
- SSE Water exceeds TMS’ payment of £30 for not meeting the service levels for response times in respect of written complaints. SSE Water offers £50 as an automatic payment for not reaching these service levels;
- In relation to low pressure, SSE Water offers a payment of £50 in instances of low pressure compared to TMS’ offering of £30. (Both of these are higher than the minimum payment under the GSS Regulations); and
- If notice is not given at least 48 hours before a planned interruption to supply (expecting to last more than 4 hours), SSE Water offers an automatic payment of £35 for household customers, whereas TMS offers £30.

However, SSE Water does not propose to match TMS in some ways, for example:

- SSE Water does not currently offer such an extensive range of services as TMS for customers with special needs. For example, TMS offers a 24 hour textphone service for hard of hearing customers, coloured background bills for dyslexic customers, and an email service for screen-reading software users;
- The opening hours for SSE Water’s bill enquiries line are not as long as TMS’ (8am-8pm Monday to Friday and 8am-6pm on Saturday, whereas SSE Water offers 8am-8pm Mon-Fri and 8am-2pm Sat);
- SSE Water does not offer as extensive a range of payment options as TMS, although the range it does offer is considered adequate;
- TMS offers free water saving devices whereas SSE Water does not. However as this site consists of new build properties, water-efficiency fittings have already been installed in the properties; and
- TMS offers a customer assistance fund for customers in debt, whilst SSE Water does not have an assistance fund.

While the areas in which SSE Water does not propose to match TMS are not statutory or appointment requirements, we have explained to SSE Water that these areas must be kept under review as its customer base expands. As SSE Water extends into different incumbent company areas and as SSE Water’s customer base grows, all Codes will be assessed against other incumbents’ policies, at which point we might request any improvements we consider necessary.

Having considered SSE Water’s overall proposed service levels, and compared them with those of TMS, we are satisfied that customers on the Site will receive a

level of service that is comparable with the level of service that they would have received had they been served by TMS.

Developer choice

Ofwat takes into consideration the choices of the site developer. In this case, the Site developer has said that it wants SSE Water to be the water and sewerage company for the Site.

Environment Agency and Drinking Water Inspectorate (DWI)

We take the views of these organisations into account before progressing to consultation on an application for a new appointment. The EA and the DWI have informed us that they are content for us to consult on this application.

TMS' existing customers

In considering whether customers will be no worse off, we also considered the potential effects of this variation on the prices that TMS' existing customer base may face.

The calculation necessarily depends on a range of assumptions, and there are clearly difficulties involved in quantifying the effect. It is therefore necessary to use a simplified set of figures. We have expressed the effect in 'per bill' terms to try and quantify the possible effect in an easily understandable way.

Broadly, we have assessed the potential magnitude of this impact by comparing how much TMS might have expected to receive in revenue from serving the Site directly, with the revenues they might expect from serving the Site indirectly via a bulk supply agreement with SSE Water. The lower bound of the range takes into account the benefit to TMS as a result of SSE Water serving the Site, by estimating the costs that TMS are likely to avoid, such as retail costs and capital and operating costs associated with the local network used to serve the Site. The upper bound of the range does not take these avoided costs into account. We look at these differences in revenue and costs over a hundred year timeframe to reflect the long life of the assets that will be used to supply customers at the Site.

In this case, we have calculated that if we grant the Site to SSE Water, there may be a potential impact on the bills of Thames Water's existing customers of between £0.00 and £0.01.

We are comfortable that these ranges account for the uncertainty in the costs that may be avoided by Thames Water.

Further, this impact does not take into account the potential spillover benefits to customers arising from dynamic efficiencies achieved as a result of the competitive process to win new sites. We set out the wider benefits we believe stem from the new appointments and variations regime below.

Wider benefits

The new appointment and variation mechanism provides a means for companies from outside the water and sewerage sectors to enter the market and for existing water and sewerage appointees to expand their businesses.

Entry and expansion (and even the threat of such by potential competitors) can lead to benefits for different customers in different ways (such as developers of new housing sites and household and non-household customers). Examples of benefits delivered via the new appointment and variation mechanism include price discounts, better services, environmental improvements and innovation in the way services are delivered. Benefits can also accrue to the existing appointee's customers, because when that appointee faces a challenge to its business that challenge can act as a spur for it to raise its game.

These wider benefits that we believe stem from the new appointments and variations regime are set out more fully in our [policy statement](#).

Overall assessment of effect on customers

Overall, we consider that customers on the Site will be at least no worse off with this Site being served by SSE Water than they would have been had the Site been served by TMS. We consider that the potential effect on TMS' existing customers is negligible or positive and in any event is likely to be offset by the wider benefits of the new appointment and variation mechanism. We are therefore satisfied that customers would be no worse off as a result of our granting this variation.

Ability to finance and properly carry out its functions

We have statutory duties to ensure that efficient appointees can finance the proper carrying out of their functions and to ensure that those functions are properly carried out. When a company applies for a new appointment or variation, it must satisfy us

that it is able to carry out all of the duties and obligations associated with being an appointed water or sewerage company.

In this case, SSE Water has satisfied us that it can finance its functions and that it is able to properly carry them out

Conclusion and next steps

In assessing SSE Water’s application for this variation, we have considered the general benefits of new appointments. We are satisfied that our two key policy principles have been met in this case, as customers will be no worse off, and SSE Water will be able to finance and carry out its functions. We have also considered the effects of granting this variation on the existing customers of TMS.

We are therefore minded to grant the appointment under the unserved criterion. We are consulting on our proposal to do so.

Where to send submissions

Any representations about, or objections to, this proposal should be sent in a single written submission to the Case Management Office, Ofwat, Centre City Tower, 7 Hill Street, Birmingham, B5 4UA or emailed to Richard.Field@ofwat.gsi.gov.uk to be received no later than 6 July 2016.