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## **Proposal by the Water Services Regulation Authority (Ofwat) to vary the Appointments of SSE Water Ltd and Thames Water Utilities Limited (Thames Water) 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 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**

SSE Water Ltd has applied to be the water and sewerage services company for a development consisting of 2,446 household properties at a site called Kingsbrook, in Aylesbury (the Site). The Site is at present within the Water Supply Area and Sewerage Services Area of Thames Water. SSE Water Ltd expects the Site to be fully developed by 2026.

### **The proposal**

Ofwat proposes to:

- vary the appointment of SSE Water Ltd as a water and sewerage company by adding the Site to its Water Supply and Sewerage Services Areas, and;
- vary the appointment of Thames Water as a water and sewerage company by excluding the Site from its Water and Sewerage Supply Areas.

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

## Policy for new appointments and variations

The new appointment and variation mechanism, set out in primary law<sup>1</sup>, 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

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<sup>1</sup> 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 Ltd 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. The Site is a new development and SSE Water Ltd submitted a letter from Thames Water which confirmed its view that the Site is unserved for water and sewerage services. Having considered the information that we have received about the Site, we are satisfied that the Site is unserved.

## **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 supplier<sup>2</sup>.

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<sup>2</sup> 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

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 Ltd will take a bulk supply of water from Thames Water to supply the Site, and will discharge from the Site into Thames Water's sewers.

SSE Water Ltd will match Thames Water's fixed and volumetric water and sewerage charges.

Having considered SSE Water Ltd'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 Thames Water.

Currently, SSE Water Ltd's conditions of appointment provide that SSE Water Ltd may not charge customers more than the charges of the previous incumbent company. In this case, SSE Water Ltd will not be able to charge customers on the Site more than Thames Water's charges for water and sewerage. We consider that, given SSE Water Ltd's small size, this represents a more proportionate way of regulating its prices than subjecting it to a full bespoke price review as we do for larger companies. However, condition B of SSE Water Ltd's conditions of appointment allows us to set a specific price limit for SSE Water Ltd. This condition is temporarily suspended but we will activate it when we consider it is appropriate to do so. This is unlikely to be before 2019.

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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.

## **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 Ltd 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 Thames Water 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 Ltd's Codes of Practice, and are content that these are of an approvable standard so customers on the Site would be no worse off than if they had been served by Thames Water.

## **SSE Water's voluntary standards**

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

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

- SSE Water Ltd offers £35 compensation if a customer regularly receives heavily discoloured water, whereas Thames Water do not offer compensation in these circumstances;

- SSE Water Ltd matches Thames Water's payment for failing to keep appointments (without giving the customer 24 hours' notice). Both companies offer £50;
- SSE Water Ltd also offers several additional standards which Thames Water does not offer. For example, SSE Water Ltd 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 Ltd matches Thames Water's 10 working day service level for the number of days taken to respond to billing enquiries;
- SSE Water Ltd exceeds Thames Water's payment of £30 for not meeting the service levels for response times in respect of written complaints (SSE Water Ltd offers £50 as an automatic payment for not reaching this service level);
- In relation to low pressure, SSE Water Ltd offers a payment of £50 in instances of low pressure compared to Thames Water's 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 Ltd offers an automatic payment of £35 for household premises and £50 for non-household premises within 20 working days compared to Thames Water's offering of £30.

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

- SSE Water Ltd does not currently offer such an extensive range of services as Thames Water for customers with special needs. For example, Thames Water 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 Ltd's bill enquiries line are not as long as Thames Water's (8am-8pm Monday to Friday and 8am-6pm on Saturday, whereas SSE Water Ltd offers 8am-8pm Mon-Fri and 8am-2pm Sat);
- SSE Water Ltd does not offer as extensive a range of payment options as Thames Water, although the range it does offer is considered adequate;
- Thames Water offers free water saving devices whereas SSE Water Ltd does not. However as this site consists of new build properties, water-efficiency fittings have already been installed in the properties; and
- Thames Water offers a customer assistance fund for customers in debt, whilst SSE does not have an assistance fund.

While the areas in which SSE Water Ltd does not propose to match Thames Water are not statutory or appointment requirements, we have explained to SSE Water Ltd

that these areas must be kept under review as its customer base expands. SSE Water Ltd has committed to do so. As SSE Water Ltd extends into different existing appointees' areas, all Codes will be assessed against other existing appointees' policies and we will request improvements we judge are required as its customer base grows.

Having considered SSE Water Ltd's overall proposed service levels, and compared them with those of Thames Water, 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 Thames Water.

## **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 Ltd to be the water and sewerage company for the Site.

## **Environment Agency (EA) 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. Both EA and DWI informed us that they are content for us to consult on this application.

## **Thames Water's existing customers**

In considering whether customers will be no worse off, we also considered the potential effects of this variation on the prices that Thames Water's 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 Thames Water might have expected to receive in revenue from serving the Site directly, with the revenues they might expect from serving the Site indirectly via bulk supply and bulk discharge agreements with SSE Water Ltd. The lower bound of

the range takes into account the benefit to Thames Water as a result of SSE Water Ltd serving the Site, by estimating the costs that Thames Water 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 Ltd, there may be a potential impact on the bills of Thames Water's existing customers of between £0.00 and £0.04.

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 Ltd than they would have been had the Site been served by Thames Water. We consider that the potential effect on Thames Water's existing customers is very 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 Ltd 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 Ltd'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 Ltd 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 Thames Water.

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 Richard Field, Senior Associate, Ofwat, Centre City Tower, 7 Hill Street, Birmingham, B5 4UA so as to be received no later than 6 July 2016. Submissions can also be emailed to: [Brian.Caire@ofwat.gsi.gov.uk](mailto:Brian.Caire@ofwat.gsi.gov.uk)

