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Trust in water

Derogations Response - summary of responses on further consultation

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About this document

This document sets out our response following a short additional consultation on our Derogations Guidance between 3 February and 10 February 2017. **Having considered responses to this consultation, we are not proposing to make changes to the derogations policy that we consulted on.**

Contents

About this document.....	2
1. Background.....	4
2. Responses from final consultation	5
3. Next Steps	8

1. Background

A derogation is a direction from Ofwat which relieves a licensee or appointee from compliance with certain of its obligations under the Wholesale-Retail Code (WRC). These obligations apply in Wholesale Contracts between wholesalers and licensed retailers and also where relevant to written arrangements between businesses in an integrated appointee, as required by Condition R4 of an appointee's Instrument of Appointment (the "Stapling Condition").

The water sector has worked with us to develop the WRC, a statutory code which sets out the terms and conditions of contracts between wholesalers and retailers and the underlying processes and operational arrangements that will govern the retail market for the supply of water and wastewater services to business customers¹.

As part of our duties as an economic regulator it is important that we consider proportionality when we monitor company compliance with the WRC. In addition, we do not want to stifle innovation in the expanded retail market.

Given:

- the different scale and sizes of companies within the water sector;
- the different scope of the competitive market in areas governed by Welsh Government policy; and
- the different commercial structures of companies within the water sector,

it is possible that instances will occur where certain companies will consider compliance with the obligations in the WRC to be disproportionate or inappropriate or where short term compliance is not possible. In these instances, derogations from compliance with certain obligations may be appropriate.

We have now completed the consultation process for our derogations policy and are issuing with this response document our Derogations Guidance, together with the electronic submission form.

¹ When we refer to business customers this includes all eligible non-household customers. Non-household customers could include businesses, public sector organisations and charities.

2. Responses from final consultation

Below we summarise the responses received from the final consultation which took place to ensure that the derogations policy changes resulting from the restructure of of Schedule 8 to ensure this had not raised any additional concerns.

The consultation questions are set out below:

Consultation questions

1. Has the restructure of the WRC and MAC caused any additional issues that are of concern?
2. Do you agree to our proposed approach to derogations within schedule 8 of the MAC given the restructuring?

We received 6 responses to the consultation. No issues were raised arising from the restructure and there was general agreement that the proposed format of schedule 8 of the MAC was a sensible and practical mechanism for implementation of derogations pending a future review.

Has the restructure of the WRC and MAC caused any additional issues that are of concern?

All respondees felt that the restructuring of the WRC and MAC had not caused any additional issues. One supported the concern we raised as part of the consultation that schedule 4 to the WRC may become unwieldy and that there should be a review in due course to assess the impact and implementation of derogations to consider whether an alternative to the proposed format of Schedule 8 may be required.

Do you agree to our proposed approach to derogations within schedule 8 of the MAC given the restructuring?

All respondents agreed with the proposed approach to derogations within schedule 8 of the MAC. Two responses highlighted that a review of schedule 8 derogations (possibly in early 2018) would be beneficial as the operation of the market will be better understood by then and the reality of market operation feeds through into code changes. A review of derogations could provide useful feedback on how to improve the WRC.

As part of the consultation we stated that we intend to monitor derogation requests and their implementation where granted, and if the volume or nature of the derogations were to become an issue, we would consider another mechanism to implement such derogations.

Additional comments

One stakeholder raised some additional comments with regards to the derogations process/application and how it needs to consider the following:

- Level Playing Field: Derogations should be tested to ensure that they have no material impact on a level playing field.
- Cost of compliance – they also raised the potential costs of derogations and ensuring compliance continues.
- The stakeholder highlighted that the impact of derogations on customer service or protection needs considering and avoiding if possible.

We agree that the above are important and these have been built into the derogations application process. In addition to this process, as derogations will also go through the enduring Panel we believe there are sufficient checks and balances in place to ensure the concerns above are considered.

The same stakeholder commented that there is a need for ongoing monitoring of derogations which are subject to “triggers” to ensure that a derogation terminates when the relevant trigger is reached. When such derogations are granted Ofwat expects the terms under which the derogation is granted to be kept under review.

This stakeholder also asked about the consultation of third parties and who these third parties may be. As Ofwat states in the guidance document we are providing flexibility in our consultations process to ensure the correct parties are consulted for example, but not limited to:

- the Market Operator;
- Defra;

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- The Welsh Ministers;
 - other Licensees and Appointees;
 - industry stakeholders, including the Drinking Water Inspectorate, Environment Agency, CCWater; and
 - any independent party for expert assessment

3. Next Steps

As a result of this final consultation, alongside this response document we are issuing the following:

- Final Derogations Guidance
- Electronic derogations submission form

We are shortly expecting to issue the final forms of the WRC and MAC which will come into effect on Market Opening.

Whilst companies may apply for a derogation prior to Market Opening no derogations will be granted prior to this date. For a derogation to be granted it would need to be considered as outlined in the guidance by the enduring codes Panel which will only be in place post Market Opening.

Unless a derogation from compliance with a specific obligation in the WRC is granted by Ofwat, all Licensees and Appointees are expected to comply with all relevant obligations in the WRC. Derogations will not be granted retrospectively and Ofwat will still consider whether enforcement action for non-compliance is appropriate in the circumstances in accordance with our [approach to enforcement](#).