

29 March 2017

Trust in water

Modifications to Albion Eco Limited's Instrument of Appointment for Retail Market Opening

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About this document

Instruments of Appointment (IoAs) are the regulatory instruments of regional water and wastewater companies (appointed companies, or appointees), containing a number of conditions which cover both retail and wholesale activities of the appointed company.

Alongside this document we have issued a Notice to modify the conditions of appointment of Albion Eco Limited's IoA. The Notice, which takes effect from the date the business retail market opens on 1 April 2017, is issued under s55 Water Act 2014 (WA14) and can be viewed [here](#).

This Notice confirms that we have modified that IoA to introduce three new conditions and amend some of the existing conditions, in advance of the extended retail market for business customers which is opening on 1 April 2017.

Under section 55 WA14 the Water Services Regulation Authority (Ofwat) may modify the conditions of an appointment under Chapter 1 of Part 2 of the WIA91 where we consider it necessary or expedient to do so in consequence of provision made by or under Part 1 of WA14.

In accordance with section 55, we [consulted](#) Albion Eco Limited (Albion Eco), together with the Secretary of State, Welsh Ministers and wider stakeholders. Having fully considered the two responses we received to that consultation, in addition to the [modifications](#) we made to other companies' IoAs in August 2016, we modified Albion Eco's IoA on 29 March 2017 for the reasons set out in this Notice. Details of the modifications are included in the Appendix, and a copy of the [specific modifications](#) is available on our website.

This document serves as both the Notice required under section 195A of the Water Industry Act 1991 (WIA91) setting out the reasons for the modifications, and the response document to the statutory consultation. Sections 2 and 3 of the document meet the requirements of section 195A and section 4 provides a summary of responses and our conclusions.

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1. Background

The WA14 will allow eligible business, charity and public sector customers (business customers) to choose their supplier of water and wastewater retail services from 1 April 2017. For customers who use the supply system or sewerage system of an appointed company whose area is wholly or mainly in England, the market will be extended to include all eligible business customers. For those who use the supply system of an appointed company whose area is wholly or mainly in Wales, only customers using more than 50 Ml of water each year will be able to choose their water supplier, reflecting the policy position of the Welsh Government.

There are two types of regulatory instrument for the expanded retail market: the new retail licences known as Water Supply and Sewerage Licences (WSSLs), and the instruments for appointed companies, which are called the Instruments of Appointment (IoAs). Defra has already consulted on, and published, the [Standard Conditions](#) of the WSSL, which will place a number of obligations on licensed WSSL retailers.

As part of the preparation for the business retail market, we considered whether any modifications to the IoAs were required to reflect the changes in legislation and/or the new market arrangements. This included, where applicable, considering possible changes for companies that have successfully applied for an appointment to replace the existing appointed water and/or sewerage company at a particular site ('new appointees').

An IoA covers both retail and wholesale activities of the appointed company. When the expanded retail market opens, appointed companies whose supply systems are wholly or mainly in England may apply to exit from the business retail market. If an appointed company exits, they would no longer need obligations in their IoA relating to their retail activities, although they would still require any obligations that are relevant to their role as a wholesaler in the market.

1.1 Consultation to date

In 2016, we separately consulted on, and implemented changes to all other companies' IoAs, as set out in the [summary document](#) (which details the observations made by stakeholders, and Ofwat's response to that consultation, which we do not repeat here).

In August 2016, Ofwat [implemented changes](#) to the conditions of all existing appointed companies' instruments of appointment. Albion Eco's appointment was granted on 28 July 2016. As our statutory consultation with the other appointed companies on the proposed changes was not concluded until 12 August 2016, we were unable to reflect these changes in Albion Eco Limited's appointment when it was originally granted.

As the changes are required ahead of the retail market opening for all eligible business, charity and public sector customers in April 2017, we now propose to make similar modifications to Albion Eco's IoA, to bring it into line with the IoAs for all other appointed companies. Ofwat published a [consultation on these proposed modifications](#) on 16 March 2017.

This document sets out the results of that consultation. We summarise the responses received, how we have considered the points made in the responses and the decision that we have reached. Alongside this document, we have published the [formal notice](#) setting out the modifications to Albion Eco's appointment.

The changes will take effect from 1 April 2017.

1.2 Aim of the proposed changes

On 16 March 2017, we published a [proposal to modify Albion Eco's IoA](#) to prepare for the opening of the retail market in April 2017. These changes would become effective at market opening, on 1 April 2017 and will:

- Help **establish the new market framework** by requiring all appointees to comply with the provisions of the Market Arrangements Code ([MAC](#)) and the Customer Protection Code of Practice ([CPCoP](#)). The changes will also require appointees which do both wholesale and non-household retail activities to apply the provisions of the proposed Wholesale-Retail Code ([WRC](#)), which will govern the behaviour and interactions of wholesalers and retailers in the market, between their wholesale and retail businesses;
- **Update definitions and other terminology** to reflect changes in legislation and to facilitate the insertion of the proposed new conditions; and
- **Extend the obligation to make drought payments** to all affected customers, regardless of whether they are customers of the appointee or a licensed retailer.

Although we have introduced a new requirement for a **separate Certificate of Adequacy** for appointees' non-household retail businesses, so that appointees face

similar obligations to licensed retailers **we proposed to exempt Albion Eco from this requirement**, as we have exempted other appointees with small numbers of eligible customers from this requirement;

2. Summary of the modifications

Table 1 – Added new conditions

Condition	Effect of the changes
MAC condition	This gives effect to the Market Arrangements Code (MAC). As it is not a statutory code, we need to give effect to the MAC via the retail WSSLs and IoAs. A similar condition is already included in the WSSL Standard Conditions. The MAC condition has been inserted into the IoAs for all appointees.
Stapling condition	This requires appointed companies which do both wholesale and non-household retail activities (integrated appointees) to apply the provisions of the Wholesale-Retail Code (WRC), which governs the behaviour and interactions of wholesalers and retailers in the market, to the arrangements between their wholesale and non-household retail activities.
Customer protection condition	This requires appointees to comply with the Customer Protection Code of Practice (CPCoP). A similar condition is already included in the WSSL Standard Conditions. This will not apply if an appointee exits the retail market.

Table 2 – changes to existing conditions

Condition	Effect of the changes
Terminology	Some changes have been inserted in Condition A and the terminology updated in Condition R to reflect legislative changes, and to add the definitions required as a consequence of the other modifications.
Condition F6	Creates a new obligation for a separate certificate of adequacy for the eligible non-household retail business of the appointee. This has been carved out of the existing obligation to have a certificate of adequacy for the whole appointed business. To be proportionate, this change does not apply to appointees with small numbers of eligible customers i.e. new appointees, appointees wholly or mainly in Wales, and Cholderton and District Water. So Albion Eco Limited has an exemption from this requirement, as it is both a new appointee and is based wholly or mainly in Wales.
Condition Q	As the obligation to make drought payments relates to the appointee's role as a wholesaler, this change extends the obligation to make the payments to all affected business customers, regardless of whether they are customers of the appointee's own retail business or customers of a WSSL

Condition	Effect of the changes
	retailer. WSSL retailers would be required to pass on the payment to the customer in accordance with paragraph 2.4.3 of the Business Terms in the WRC

3. Why were the modifications necessary?

The changes were required to:

- Establish the new market framework by requiring all appointees to comply with the provisions of the proposed **MAC**, the **WRC** and the **CPCoP**;
- Reflect changes in legislation, especially the provisions of the WA14;
- Remove duplication and potential inconsistencies between the IoAs and **WRC** and **MAC** in relation to a number of other conditions; and
- Introduce a new requirement for a separate Certificate of Adequacy or Ring-fencing Certificate for all appointees' non-household retail businesses, so that all appointees face similar obligations to licensed retailers.

3.1 MAC condition

This new condition has been inserted into the IoAs to require all appointees to give effect to, and comply with the MAC. A similar condition is already included in the standard conditions for WSSLs.

The MAC condition is required to help create the legal framework and give effect to the MAC on an enduring basis, as the MAC is not a statutory code. By inserting a collective obligation in the IoAs and WSSLs, appointees and licensees are required to create the MAC in accordance with the provisions of the condition, so ensuring that the MAC will be in existence at market opening. Similarly these parties are required by the condition to sign the Framework Agreement which will give effect to the MAC, ensuring all parties are contractually bound by its provisions. Appointees and licensees are required to comply with the provisions of the MAC on an ongoing basis and to maintain the MAC in accordance with the provisions in the condition.

Additionally, the MAC condition confirms certain essential elements of market governance, including the code change process. It is necessary for the MAC condition to do this ahead of market opening, so that the essential market governance arrangements required to ensure the correct operation of the market balance the interests of market participants at the outset and cannot be changed or removed without Ofwat having an opportunity to veto the change or change the conditions of relevant undertakers or licensees.

Once the retail market has opened and the market governance arrangements are properly embedded, we intend to review the MAC condition as part of our longer term plan of simplifying IoAs by moving towards a principles based approach to

licences and IoAs. At that stage, it may be possible to strip out some of the more detailed provisions about market governance while retaining the essential elements of the legal framework, provided those governance arrangements are suitably established and working well.

3.2 Stapling condition

This new condition has been added to require appointees with integrated wholesale and retail businesses to apply the provisions of the WRC to arrangements between their wholesale business and their retail business for eligible business customers. This was required to support the effective functioning of the competitive business retail market and is in the best interests of customers, as the WRC would not otherwise apply to those arrangements. As Albion Eco is an integrated wholesale and retail business, it is important that this condition is included within its IoA.

3.3 Customer protection condition

This new condition has been inserted in the IoAs to protect eligible business customers in relation to a number of retail activities by requiring appointees to comply with the recently published [CPCoP](#). A similar condition is already included in the WSSL standard conditions. This condition would not apply to an appointee that exits the retail market.

3.4 Condition Q amendments

Condition Q relates to interruptions to supply because of drought. This amendment was required to reflect the fact that once the business retail market opens, the appointee may not directly supply all customers potentially affected by drought, as it is anticipated that some eligible customers would be supplied by one or more WSSL retailers. The definition of business customer in this condition needed to be updated to include all customers that are supplied by the appointee acting as a wholesaler, even though some of them may have their retail contract with a WSSL retailer. This means that the appointee, acting as a wholesaler, would be required to make drought payments to all affected customers within its area of appointment, rather than just its own retail customers. Customers who decide to switch to another retailer are not disadvantaged and do not lose the protection provided by this condition.

3.5 Condition F6.2A or F6.2 - separate certificate of adequacy or ring-fencing certificate

Appointees are required to provide a certificate of adequacy or ring-fencing certificate for their whole appointed business. We modified the IoAs of other appointed companies to require a separate certificate in respect of the appointee's retail business for eligible business customers, carved out of the existing obligation. This modification was necessary to provide parity between WSSL retailers and the retail businesses of appointed companies, to help create a level playing field in the business retail market. The WSSL standard conditions already include a similar obligation to provide a certificate of adequacy in respect of the licensee's retail business. This means that appointees are required to provide a certificate for their retail business for eligible business customers, and a certificate for the rest of their appointed business. This would not apply to an appointee that exits the retail market.

However, on the ground of proportionality, this modification has not been made for appointees with small numbers of eligible customers i.e. new appointees, Cholderton and District Water, and appointees wholly or mainly in Wales. So Albion Eco has an exemption from this requirement, as it is both a new appointee and is based wholly or mainly in Wales.

3.6 Condition R and A – terminology and new definitions

New definitions have been added to reflect changes in legislation, to provide consistency with the WRC and MAC, and in consequence of the other modifications made. Some amendments to Condition R have been made to reflect those new definitions and changes in legislation.

4. Responses to the consultation

4.1 Albion Eco

Albion Eco responded to the consultation confirming that it is content for its IoA to be amended so as to mirror those of all other appointed companies. Albion Eco did raise one concern in its response, which is around an issue that arises as a consequence of the modifications, rather than a concern around the modifications themselves. The concern relates to the charging arrangements established by MOSL for retailers.

Essentially, the concern is that there is a minimum fixed market operator charge, in Schedule 6 of the MAC, of £250 a month for undertakers in relation to their Retailer Business' share of the Retailer Market Operator Charges, which means that Albion Eco, who has just one eligible customer at present, will be required to pay ~£3,000 per annum in relation to that single customer, whereas large regional incumbents with multiple customers are likely to pay less than £1 per eligible customer. Albion Eco considers that the current fee calculation could be seen as producing anti-competitive charges and could act as a barrier to new and small retailers. We [consulted](#) on the provisions in Schedule 6 of the MAC last year and this particular matter was not raised. In terms of addressing any outstanding issue, we consider that it is for MOSL and market participants, in the first instance, to consider how best to resolve this and to propose any subsequent modification to the MAC, if appropriate.

4.2 Other responses

CC Water responded to our proposed modifications with no comments, noting that the proposed modifications would raise no concerns for customers.

Under s55 of the WA14, we are required among other things to consult the Welsh Ministers and the Secretary of State, who may direct us either not to make the proposed modifications or to amend them as directed. As part of this consultation, we wrote to Welsh Ministers and the Secretary of State seeking their views on the proposed modifications. Defra has confirmed that it had no comments in relation to these modifications. We received no comments or objections from Welsh Government on the proposed modifications to Albion Eco's IoA.

4.3 Our confirmed approach

Having considered fully the responses received in relation to this consultation, we have decided not to make any changes to our proposed modification of Albion Eco's IoA. Consequently, we have modified Albion Eco's IoA for the reasons set out in this Notice. [A copy of the specific modifications](#) is available on our website.