

16 March 2017

Trust in water

Proposal to modify Albion Eco Limited's Instrument of Appointment under section 55

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About this document

This document invites comments on our proposals to modify Albion Eco Limited's Instrument of Appointment to introduce three new conditions and amend some of the existing conditions, in advance of the expanded retail market for business customers which is opening in April 2017. These changes have already been made to all other companies' Instruments of Appointment.

Under section 55 of the Water Act 2014 (WA14) the Water Services Regulation Authority (Ofwat) may modify the conditions of an appointment under Chapter 1 of Part 2 of the Water Industry Act 1991 (WIA91) where it considers it necessary or expedient to do so in consequence of provision made by or under Part 1 of WA14.

This consultation fulfils our requirement under section 55 to consult the holder of the IoA that we propose to modify, together with the Secretary of State, Welsh Ministers and anybody else we think is appropriate.

Although there are no statutory provisions with regard to the length of the consultation period, we are bound by our wider public administrative law duties. In the circumstances of the particular modifications proposed in this consultation, we consider 6 working days to be appropriate and proportionate in view of the:

- Prior consultation on this matter; and
- The nature of the modifications.

Subject to responses to this consultation, including any statutory response from the Secretary of State or Welsh Ministers received within the consultation period, we plan to modify Albion Eco Limited's Instrument of Appointment by the end of March 2017. The finalised conditions would take effect when the retail market opens.

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Responding to this consultation

We invite stakeholders to comment on our intended modifications by **24 March 2017**. Please email your responses to daniel.mason@ofwat.gsi.gov.uk or post them to:

Retail Market Opening Programme
Ofwat
21 Bloomsbury Street
London WC1B 3HF.

If you wish to discuss any aspect of this document, please direct your enquiry to Dan Mason on 0121 644 7629 or by email to daniel.mason@ofwat.gsi.gov.uk.

We will publish responses to this document on our website at www.ofwat.gov.uk, unless you indicate that you would like your response to remain unpublished. Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with access to information legislation – primarily the Freedom of Information Act 2000 (FoIA), the Data Protection Act 1998 and the Environmental Information Regulations 2004. If you would like the information that you provide to be treated as confidential, please be aware that, under the FoIA, there is a statutory 'Code of Practice' which deals, among other things, with obligations of confidence. In view of this, it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information, we will take full account of your explanation, but we cannot give an assurance that we can maintain confidentiality in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on Ofwat.

1. Introduction and summary of proposals

1.1 Background and purpose

The WA14 will allow eligible business, charity and public sector customers (business customers) to choose their supplier of water and wastewater retail services from April 2017. For customers who use the supply system or sewerage system of a regional monopoly water company (appointed company) whose area is wholly or mainly in England, the market will be extended to include all business customers. For those who use the supply system of an appointed company whose area is wholly or mainly in Wales, only business customers using more than 50 Ml of water each year will be able to choose their water supplier, reflecting the different 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 preparations for the retail market, we need to make some changes to the IoAs. At the moment, an IoA covers both the retail and wholesale activities of appointed companies, but when the expanded retail market opens those appointed companies whose areas 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 remain subject to obligations that are relevant to their role as a wholesaler in the market.

In 2016, we separately consulted on, and implemented changes to all other companies' IoAs as set out in the [summary document](#).

Albion Eco Limited (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, we were unable to reflect the changes in Albion Eco's appointment when it was originally granted.

As the changes are required ahead of retail market opening 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.

This consultation document describes the proposed changes to Albion Eco's IoA and explains why we need to make them.

1.2 Aim of the proposed changes

We propose to modify Albion Eco's IoA as set out in this consultation to prepare for the opening of the retail market in April 2017. Although we propose to modify the IoA by the end of March 2017, subject to responses to this consultation, the changes would only be effective at market opening, on 1 April 2017.

The changes will:

- Help **establish the new market framework** by requiring all appointees to comply with the provisions of the proposed 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;
- 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 propose to exempt Albion Eco from this requirement**, as we have exempted other appointees with small numbers of eligible customers from this requirement;
- **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.

1.3 Summary of proposals

Table 1 – Proposed new conditions

Condition	Proposed approach
MAC condition	This will give effect to the MAC . As it is not a statutory code, we need to give effect to the MAC via the retail Water Supply and Sewerage Licences (WSSLs) and IoAs. A similar condition is already included in the

	WSSL Standard Conditions . We propose to insert the MAC condition into the IoA so that all appointees have this condition.
Stapling condition	This will require appointed companies which do both wholesale and non-household retail activities (integrated appointees) to apply the provisions of the WRC , which governs the behaviour and interactions of wholesalers and retailers in the market.
CPCoP	This will require appointees to comply with the recently published CPCoP . A similar condition is already included in the WSSL Standard Conditions .

We also propose to amend some of the existing conditions.

Table 2: Proposed amendments to existing conditions

Condition	Proposed change
Terminology	Some changes to Condition A and Condition R will be required to reflect the legislative changes, and to update the definitions to reflect the other changes proposed in this consultation.
Condition F6	To create a new obligation for a separate certificate of adequacy for the (eligible) retail business of the appointee. This will be carved out of the existing obligation to have a certificate of adequacy for the whole appointed business. To be proportionate, this change will 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 will be given 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, we propose to extend 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 retailer.

1.4 Consultation process to date

We initially consulted on proposals to amend the IoAs in June 2015, as part of our wider licensing proposals in preparation for retail market opening. Since then, we have developed and refined our proposals with input from appointees and other stakeholders through a process of consultation over a number of months. In the meantime, the [Standard Conditions](#) for the WSSLs have been finalised and published, which include some conditions that are nearly identical to some of the conditions that we propose to insert in the IoAs.

In May 2016, we published a consultation on changes to all the IoAs ([May consultation](#)) and held workshops to discuss our draft proposals, including workshops for appointed companies with small numbers of eligible customers (including new appointees, and those whose systems are wholly or mainly in Wales).

As a result of comments received in response to the May consultation and during discussions at the workshops, we reviewed and updated our proposals and published a further consultation ([June consultation](#)) to provide appointed companies and other stakeholders with an additional opportunity to comment on the updated draft text for the IoAs. We received ten responses to the June consultation, with some suggestions for improving the draft text further.

Having considered all the comments and suggestions, we reviewed and refined our proposals, and then consulted companies on [our final proposals](#) under section 55 of the WIA14 in July 2016 (the statutory consultation). Following that consultation, we [implemented the changes](#) for all other appointees in August 2016, by modifying the IoAs.

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, we were unable to reflect these changes in Albion Eco's appointment when it was originally granted.

As the changes are required ahead of retail market opening 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.

This consultation sets out the changes to Albion Eco's IoA that we propose to make under s55 of the WA14.

1.5 Structure of this document

The rest of this document is set out as follows:

- Chapter 2 provides details of the three new conditions that we propose to insert;
- Chapter 3 provides details of the proposed amendments to some of the existing conditions in the IoA;
- Chapter 4 explains that we propose to make these changes under s55 of the WA14;
- Chapter 5 discusses the interaction with retail exit; and
- Chapter 6 outlines next steps.

Detailed draft text for all the proposed changes is provided in the Appendix.

2. Proposed new conditions

The proposed new conditions are set out in the attached Appendix, and have already been inserted in all other companies' IoAs.

2.1 MAC condition

We propose to insert a new condition into the IoA to require Albion Eco to give effect to, and comply with the MAC.

The draft MAC is a multi-lateral code that will apply to all market participants, regardless of whether they are acting as a wholesaler or a retailer. It contains provisions that set out how the parties will work together to govern the market and will be an essential part of the new market [legal framework](#). Among other things, it will help to establish the market operator that will facilitate the effective operation of the market. Unlike some of the other codes that form part of the legal framework for the retail market, the MAC will not be a statutory code. So we need to give effect to it using a different legal tool. We propose to do this by inserting a new condition in the IoAs, as we have done for WSSLs, requiring companies to be a party to, and comply with, the MAC with certain minimum requirements for the content of the MAC.

Responses to date

Responses to our earlier consultations were very supportive of the proposed MAC condition, with widespread recognition of the important role it will play in giving effect to the MAC, although some responses suggested that the drafting of the MAC condition could be improved. We disagreed with some of the suggested changes so they are not reflected in the final version of the condition.

2.2 Stapling condition

We propose to introduce a new condition for appointed companies which do both wholesale and non-household retail activities (integrated appointees). This will require integrated appointees to apply the provisions of the WRC to interactions between their wholesale business and their retail business for eligible business customers. This condition is referred to as the stapling condition.

Responses to date

During our earlier consultations, there was full support for this proposal in principle, although some responses suggested changes to improve the proposed drafting, which have been reflected in the final version of the condition.

Possible Code Derogations

We also considered the interaction with derogations. An agreed derogation would permit an appointee to not comply with certain specified code provisions for either an indefinite or definite time period, or in some cases would never apply at all.

There are two different, but potentially overlapping, reasons why derogations may be required. The first is based on the fact that an integrated appointee remains one legal entity, so there may be some provisions of the codes that cannot reasonably be applied because of its status as one legal entity. We expect such derogations to be very limited. The second is based on the principles of proportionality. We could not reasonably expect appointees with very small numbers of eligible customers to take all the same steps as a much larger appointee, although we would still expect any requests for derogations on the grounds of proportionality to be exceptional, compelling and evidence-based.

In developing the stapling condition we have acknowledged that it may not be appropriate for an integrated business to apply all the provisions of the WRC to the interactions between its wholesale and retail businesses.

In particular, we consider that some derogations may be required for those appointees with smaller numbers of eligible customers, especially new appointees and those whose supply system is wholly or mainly in Wales, on the grounds of proportionality. More details are included in our [guidance on derogations](#) and the [results of our separate consultation](#) on derogations.

2.3 Customer protection condition

As part of the preparation for the retail market, we have considered how to appropriately protect customers in the expanded market. The best way to protect customers is to make sure that the market works effectively in the best interests of customers, but we have also considered whether additional protections may be required in certain areas. Following a lengthy consultation process, we published the [CPCoP](#), which among other things, includes provisions on sales and marketing

activities, contracts and billing. We propose to insert a new condition in the IoAs to require appointees to comply with the [CPCoP](#). A similar condition is already included in the WSSL standard conditions.

Responses to date

Responses fully supported the proposed condition, although some comments on the drafting were received.

We updated the draft text of the condition slightly in the June consultation to be clear that it only applies to eligible business customers, in recognition of the concern raised by appointees whose supply systems are wholly or mainly in Wales. Although the application of the [CPCoP](#) as currently drafted is limited to eligible business customers, we recognise that the [CPCoP](#) may evolve in the future, so there is a justification for using the customer protection condition in the IoAs to restrict the application of the [CPCoP](#) to eligible customers. The issue does not apply for WSSLs, as their customers will only be eligible business customers, so no change would be required for the WSSL standard conditions.

3. Proposed amendments to existing conditions

In addition to the proposed new conditions outlined above, we propose to update some of the existing conditions in Albion Eco's IoA to reflect the new market arrangements. The proposed changes are marked in tracker in the Appendix, and similar changes have already been made to all other companies' IoAs.

Responses to our earlier consultations fully supported our proposal to amend some of the existing conditions.

3.1 Conditions A and R – terminology and new definitions

We propose to update the terminology in the IoA to reflect changes in legislation and in the Appendix we highlight areas where the terminology would be updated.

The proposed changes would insert new defined terms into Condition A to reflect changes to legislation and to define the necessary additional terms used in our proposed amended text as set out in this consultation:

“2014 Act” – “Water Act 2014”

“Licensee” – “the holder of a water supply licence and/or a sewerage licence granted by the Water Services Regulation Authority under section 17A and/or under section 17BA of the Water Industry Act 1991”

“Eligible premises” – shall have the meaning given in the Wholesale-Retail Code

“Retail market opening date” – means the date determined by the Authority as the date when the retail water and sewerage market for Eligible Premises opens

“Wholesale-Retail Code”- the code issued by the Water Services Regulation Authority pursuant to sections 66DA and 117F of the Water Industry Act 1991.

Some amendments to Condition R have been made to reflect those new definitions and changes in legislation.

Responses to date

Responses supported our proposal to update the terminology, although we received comments from a couple of appointees about the drafting. Some changes were incorporated in the final version of the modifications.

3.2 Condition F6 Certificate of adequacy

We propose to create a new obligation for a separate certificate of adequacy for the business customer retail business of the appointee, carved out of the existing obligation to have a certificate of adequacy for the whole appointed business. But we propose to provide an exemption to companies with limited numbers of eligible customers on the grounds of proportionality. **Albion Eco would be exempted from this requirement, so we propose no change to Condition F6.**

Responses to date

The majority of responses to our earlier consultations agreed with our proposal, although there were some comments on the drafting and two new appointees requested an exemption on the grounds of proportionality. We have since confirmed that companies with limited numbers of eligible customers (including new appointees, and those wholly or mainly in Wales) would not be required to provide a separate certificate of adequacy.

3.3 Condition Q – drought payments

As the obligation to make drought payments relates to the appointee's role as a wholesaler, we propose to extend 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 retailer.

Responses to date

Responses supported this proposal. A couple suggested that some safeguards may need to be put in place to ring-fence the payments for customers, in case the retailer becomes insolvent, to prevent the wholesaler being required to pay twice. It was noted that drought incidents can be widespread, affecting many customers, which could increase the risk of a retailer getting into financial difficulties.

We agree that we need to make sure drought payments for affected customers are passed on to those customers. As the provisions of the IoAs do not apply to retailers, we would need to find another way to implement any such safeguards, if we decide that they are required. The WRC and the WSSLs are the most likely instruments for this. We will also continue to engage with the MOSL codes working group on

leakage adjustments and drought payments, to identify what further changes may be required to the loAs, WSSLs and the codes in due course.

Finally, it should be noted that the drafting of Condition Q is also expected to be reviewed as part of Ofwat's separate project to simplify some of the conditions of the loAs.

4. Application of section 55 WA14

Sections 55(1) and (2) of the WA14 allow Ofwat to modify the conditions of an appointment of a company appointed under Chapter 1 of Part 2 of the WIA91 (i.e. an instrument of appointment) or of a licence under Chapter 1A of Part 2 of the WIA91 (currently the Water Supply Licence or WSL but, in due course will include the new water supply and sewerage licences or WSSLs), "where it considers it necessary or expedient to do so in consequence of provision made by or under" Part 1 of the WA14. This power may only be exercised within two years of the date the provision in question comes into force.

We consider that the introduction of these new conditions, and the proposed amendments to the existing conditions, are both necessary and expedient as a consequence of general provision made in relation to the business customer retail market implemented by Part 1 of the WA14 as a whole.

4.1 The expansion of the business customer retail market

The effective removal of the threshold requirement for licensees who use the supply system of appointed companies whose supply systems are wholly or mainly in England and the introduction of the sewerage licences will lead to many more customers being in the business customer retail market. The market is forecast to increase from its current size of around 20,000 customers, to around 1.2 million customers from April 2017. As the number of customers in the market increases, the need for new and effective market arrangements increases. The proposals set out in this consultation are required to give effect to the detailed market rules (codes) that will govern the new market arrangements, as well as removing some of the existing arrangements that will no longer be required. The proposed changes will remove some areas of duplication and facilitate the move from regulated access to negotiated access. Responses to our earlier consultations have been supportive of the need to make these changes in preparation for the expanded retail market.

Although the threshold requirement will remain for licensees who use the supply system of appointed companies whose supply systems are wholly or mainly in Wales, the relevant Welsh companies will still need to participate in the new market arrangements and will need to ensure that they can meet the customer data, system and process requirements of the market, albeit in a proportionate way given the limited number of eligible customers that they have in the market. These changes are important for Welsh companies to ensure that the way they interact with the system will not disadvantage them, nor will it inadvertently create competition law

risks. The increased scale and scope of requirements necessitate the introduction of a market operator and the associated market arrangements. We therefore consider that these new conditions, and amendments to existing conditions, should be introduced for all appointees, regardless of whether they are in England or Wales. Using section 55 will help to provide greater consistency between the IoAs, and certainty of implementation.

5. Managing the interaction with retail exit

Albion Eco's supply system is based wholly or mainly in Wales, so exit is not permitted. The table below summarises the application of these proposals for appointees depending on whether they exit or not, or if they are wholly or mainly in Wales.

Table 4: Summary of proposals showing the different position for appointees depending on whether they exit or not, or are wholly or mainly in Wales

Appointees wholly or mainly in England		Appointees wholly or mainly in Wales (including Albion Eco)
Exit	No exit	Exit not permitted
MAC condition	MAC condition	MAC condition
Stapling condition switched off	Stapling condition	Stapling condition (business customers using more than 50 MI only)
Customer protection condition switched off	Customer protection condition	Customer protection condition (business customers using more than 50 MI only)
Terminology changes	Terminology changes	Terminology changes
Separate certificate of adequacy provision switched off	Separate certificate of adequacy required - exemption for small companies	Exemption – no requirement for separate certificate of adequacy
Updated condition Q	Updated condition Q	Updated condition Q

6. Next steps

Albion Eco and other stakeholders, including the Secretary of State and the Welsh Ministers, are invited to **respond to this consultation by 24 March 2017**. Subject to the responses to this consultation, we plan to modify Albion Eco's IoA by the end of March 2017.

The new and amended conditions would only take effect at market opening, on 1 April 2017.