

## **Clear Business Water PR19 Response**

We welcome the opportunity to provide some input into the PR19 methodology and how your proposals are trying to drive change and innovation for the customers benefit. We are supportive of your proposals to set price controls for English Water companies that have not exited the Business Retail Market. Your proposal to run a 3-year Business Retail Price control is a move in the right direction but we would suggest a shorter review period to allow quicker reaction to how the market is progressing, maybe a 1 or 2-year price control would be more appropriate. A 2-year control would allow for a re-assessment of the market after it has been open 5 years, but unless wholesale costs are included in a review there will be limited scope for change.

However, in terms of switching we believe that the English Water Market is not working as effectively as it could, given that only 1.4% of the market switched in the first 3 months, with almost a third of that down to pre-registrations prior to market opening. A good proportion of the switching that has taken place so far appears to be SPID consolidation to bring water and waste SPID's back together, for customers who would have received separate bills for water and waste, due to the market opening.

We believe that the poor level of switching is fundamentally down to three reasons:

- Poor quality market data preventing a switch
- Lack of customer awareness that the market is open and they can switch.
- Significant lack of customer savings.

### **Poor quality market data preventing a switch**

We assume that the industry will address the quality of market data, especially around metering and meter read data. Examples that we have come across include:

- Meter Locations being recorded incorrectly.
- Meter Read History containing meter reads that appear to be estimated as transfer a lower than the latest read uploaded by a wholesaler.
- Service components missing such as tariff data.

These are issues that we raised with PWC as part of their market audit.

### **Lack of customer awareness that the market is open and they can switch**

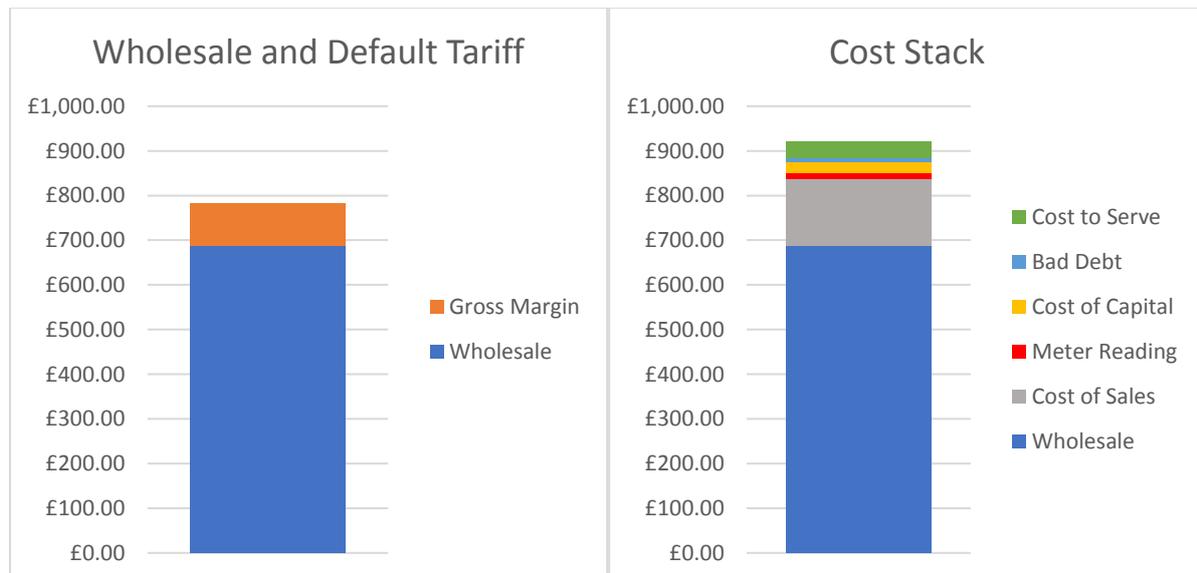
Retailers should be able to address the lack of customer awareness, but this does come at a cost and in some wholesale regions there will be very little effort to try to sell given the limited savings that could be offered. The Scottish market is a very good example where we have seen customer awareness as nearly 47% of the market have switched away from the incumbent, switching increased after regulator intervention in 2013.

### **Significant lack of customer savings**

Our main concern we feel that the regulator should be addressing is the lack of savings that a customer can achieve. Further consideration should be given to your default proposal should you

decide to continue with controls for Business Retail, as we believe that this will lead to a continuation of the current level of customer inertia and not stimulate switching, especially for SME's. We would suggest you need to review your approach with regards to the level of cost to serve and margin allocations, as well as increase pressure on wholesalers to reduce their costs. In relation to cost to serve an approach could be to look at incumbent retailer's costs and those of new entrants as well as benchmarking this figures with other comparative industries. You should also consider a minimum cost to serve to ensure that smaller customers have sufficient margin to cover fixed costs such as meter reading and producing an invoice which will take a large or in some cases all available margin. Unless this is addressed the smallest customers will be unlikely to benefit from competition, which is one Defra's strategic objectives for Ofwat. Focusing on average customers within bands means that there will be winners and losers and work must be done to ensure every customer has sufficient cost to serve and available margin to benefit from competition. You also do not include costs to acquire or retain customers in any of your costs, we suggest that these should to be considered. Given that you don't cover all costs associated we don't feel that there is a significant enough of a return on investment or capital required to compete in the English water market.

### Cost Stack



To give you an evidence of this in the left-hand side chart, we have taken the market data and worked out the average Wholesale Cost and average Default tariff that would be applicable.

In the chart on the right-hand side we have built on top of the wholesale chart to include costs, such as bad debt, meter reading, cost of capital, cost to serve and cost of sales. This doesn't include a Gross margin, but as you can see the allowable Gross Margin, doesn't cover our costs.

Our parent company Verastar serves around 150,000 SME customers and at Clear Business Water we believe that we are a lean, experienced and operationally efficient organisation, having grown to be 2<sup>nd</sup> largest retailer in the Scottish market. We have a relatively low cost to serve, but given the current pricing restrictions, we are struggling to offer customers any meaningful savings. Our experience has shown that customers are looking for at least double digit percentage savings to have an incentive to switch, this is a level that we don't believe anyone can offer to a customer.

## **GAP site & Vacants**

We would suggest that there are learnings to be taken away from the Scottish market and expect that incentives will be run for Retailers to identify GAP sites in England. It feels unfair that the rest of Business Community should be paying for water and waste that is being used by GAP sites. In Scotland, the GAP sites found in the last 2 and half years' account for just over 8% of the overall market. There is no current motivation for a wholesaler to bring these sites into the market given the revenue caps that are placed on wholesalers. Another incentive we would support is an incentive for identifying vacant sites, to support the accuracy of market data.