

30 October 2017

Trust in water

# **Proposal to grant a variation of appointment to SSE Water Limited to enable it to provide water and sewerage services to a site called White City**

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## 1. About this document

This notice is a consultation (under section 8(3) of the Water Industry Act 1991 (“**WIA91**”)), on our proposal to grant a variation of appointment to SSE Water Limited (“**SSE**”) as a water and sewerage company and vary the appointment of Thames Water Utilities Services (“**TMS**”) as a water and sewerage company.

The consultation period will last for 28 days from the date of publication of this notice. Having considered any representations submitted during the consultation period in response to the consultation, Ofwat will decide whether or not to grant a variation of appointment to SSE as a water and sewerage company.

## 2. The Site

SSE has applied for a variation to its appointment to enable it to provide water and sewerage services to a site called White City (“**the Site**”), which is in **TMS**’ water supply area and its sewerage services area.

The Site is in London, W12. When fully built, the Site will consist of 1,765 household dwellings. The first occupancy of the Site is expected to be in early 2019, when construction has been completed.

### **3. The applicant**

SSE obtained its first appointment as a water and sewerage undertaker on 1 October 2007 for a housing development called the Portway, Old Sarum in Wessex Water's area. Since then, Ofwat has agreed to vary SSE's area of appointment so that it serves a further 27 sites for water and/or sewerage services.

## **4. The proposal**

Ofwat proposes to:

- grant a variation of appointment to SSE as a water and sewerage company to include the Site in its water supply area and its sewerage services area; and
- vary the appointment of TMS as a water and sewerage company by excluding the Site from its water supply area and its sewerage services area.

By means of the above, SSE will become the water and sewerage services supplier for the Site.

## 5. Our approach to the assessment of this application

The new appointment and variation mechanism, set out in primary legislation<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 – [policy](#) and [process](#) documents. In November 2012, we published our '[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 or variation, 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 customers more generally across England and Wales, who in our view benefit from the effective operation of the new appointment and variation mechanism.

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<sup>1</sup> The legal framework for new appointments is set out in the 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.

## 6. The application

SSE has applied to be the water and sewerage company for the Site under the unserved criterion, set out in section 7(4) (b) of the WIA91.

### 6.1 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 are served by the existing appointee.

A site survey report was provided to Ofwat on 16 May 2017. The report indicates that the Site was previously commercial, but that all previously used infrastructure has been cleared. All existing buildings have been demolished, and replaced with site offices and construction storage. The site offices are served with a temporary provision, which will be removed when the developer leaves the Site. The Site is currently unoccupied, apart from the developer.

TMS has provided confirmation that in its view the Site is unserved for both water and sewerage. TMS's water and sewerage network records show that no assets cross the Site. Given this information, we are satisfied that the Site will be unserved at the time of the variation of appointment.

### 6.2 Protecting customers

Ofwat acts to protect customers, especially those who are unable to choose their supplier. In assessing applications to supply new development sites, Ofwat acts on behalf of both existing customers as well as potential new 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 and variations – only business, charity and public sector customers (“Business Customers”) in England and Wales are able to choose their supplier<sup>2</sup>.

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

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<sup>2</sup> The majority of Business Customers where the area of the relevant appointed company is wholly or mainly in England, have effectively been able to switch retail suppliers of water and sewerage from 1 April 2017. Business Customers where the area of the relevant appointed company is wholly or mainly in Wales can only switch if their premises are, or are likely to be, supplied with at least 50 MI per year.

and levels of service than if they had been supplied by the existing appointee in whose geographical area the relevant site sits. We will continue to protect customers on a site by regulating the new appointee's prices and service levels.

### **6.3 Price**

SSE proposes to charge customers on the Site charges that are equivalent to the charges of TMS. SSE proposes to match the tariffs of TMS for customers whose circumstances make them vulnerable.

### **6.4 Levels of service**

Every appointee is required under its conditions of appointment to publish Codes of Practice on debt and leakage and to have a Customer Code for its household customers. We have assessed SSE's proposed Codes of Practice and Customer Code, and our view is that these are of an appropriate standard. Our view is that customers on the Site would be no worse off in relation to the points covered by the above Codes of Practice and the Customer Code than they would be if TMS were to be the customers' water and sewerage services supplier.

### **6.5 Site owner choice**

SSE has the consent of the Site developer, St James Group, to become the water and sewerage services provider for the Site.

### **6.6 Environment Agency (EA) and Drinking Water Inspectorate (DWI)**

We take the views of these organisations into account before progressing to formal consultation on an application for a new appointment. Both the EA and DWI informed us that they are content for us to consult on this application<sup>3</sup>.

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<sup>3</sup> The Environment Agency and the Drinking Water Inspectorate will also be formally consulted on the proposals, as they are on the list of organisations which must be formally consulted as set out in section 8(4)(b) of WIA.

## **6.7 Incumbent'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 TMS' 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.

In assessing the impact that granting the Site may have on the incumbent's customers, we compare the revenue the incumbent might have been expected to receive and the maintenance costs it would expect to incur if it were to serve the Site directly, as opposed to the revenues it would receive and costs it would incur from the proposed variation arrangement.

We recently updated the approach we take to this calculation to reflect the current price setting regime and the latest financial data.

Using our updated approach, we estimate a potential £0.003 annual increase on the water bills of existing TMS customers if we grant this variation to SSE. This is once the Site is fully built out.

This estimate does not take into account the potential spill-over benefits to customers arising from dynamic efficiencies achieved as a result of the competitive process to win sites.

Therefore we consider that granting this variation to SSE would have a very small financial impact on customers' bills and could have potential benefits for customers.

## **6.8 Ability to finance and properly carry out its functions**

We have a statutory duty to ensure that efficient appointees can finance the proper carrying out of their functions. 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 and sewerage company.

We have considered the financial position of SSE in relation to providing water and sewerage services to the Site, and we are satisfied the company demonstrates sufficient financial viability.

SSE is supported by a Parent Company Guarantee (“PCG”), which meets our requirements, in that it covers one year’s annual operating costs required to supply the number of connections the business is projected to have in two years’ time.

On this basis, our view is that the risk of this Site not being financially viable is small and as a result we are currently satisfied that applicant would be able to finance its functions if the variation is granted.

## 7. Conclusion and next steps

In assessing SSE's application, we have considered the general benefits of new appointments and variations. Our view is that our two key policy principles would be met in this case, as customers would be no worse off, and SSE would be able to finance, and carry out, its functions. We have also considered the effects of granting the proposed new appointment and consequential variation on the existing customers of TMS.

We are currently minded to vary the appointment of SSE as a water and sewerage company under the unserved criterion. We are consulting on our proposal to do so.

### Where to send submissions

Any person who wishes to make representations or objections with respect to the application should do so in writing (which includes by email) to Chris Daly at Centre City Tower, 7 Hill Street, Birmingham, B5 4UA or by email at [Chris.Daly@ofwat.gsi.gov.uk](mailto:Chris.Daly@ofwat.gsi.gov.uk)

Representations must be received by Ofwat no later than 17.00 hours on 27 November 2017. Further information about how to make representations or objections, including information on the treatment of confidential information, can be obtained from Ofwat at the above address or at <http://www.ofwat.gov.uk/foi/>

Ofwat will only use the information you have provided for the purpose of this consultation. We will retain your information in accordance with Ofwat's retention schedule and will not share with third parties unless we have a legal obligation to do so. For further information please see Ofwat's Privacy Policy in our [Publication Scheme](#).

