

December 2018

Trust in water

**Conclusions on licence
simplification and modification of
all instruments of appointment**

About this document

On 19 September 2018 we published a consultation on “[Proposed modification to simplify various conditions of all undertakers' licences](#)”. The consultation closed on 19 October 2018. Our intention was to simplify and modernise the licence conditions, while maintaining the protections for customers and the balance of risk for companies.

Under section 13 of the Water Industry Act 1991 (‘WIA91’), the Water Services Regulation Authority (‘Ofwat’) may modify the conditions of a water undertaker’s (‘Appointee’s’) Instrument of Appointment (‘licence’) if the Appointee consents to the modifications. Before making modifications under section 13 of the WIA91, Ofwat must give notice in accordance with that section. The consultation was a notice under section 13.

In this document, “Conclusions on Licence Simplification and Modification of all Instruments of Appointment”, we set out the comments made in response to the consultation and how we have taken them into account in arriving at our final decision on licence modifications. This document is also a notice confirming that Ofwat has now modified the licences of all Appointees in accordance with section 13 of the WIA91 and sets out our reasons for doing so as required by section 195A WIA91. These changes will come into effect for most conditions on 1 January 2019, with Conditions F and N coming into effect on 1 March 2019.

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1. Responses to the consultation

Our consultation invited comments on the changes we proposed to make to all Appointees' licences, both as general changes and changes to specific conditions.

We received 27 responses to the consultation: 26 from the existing licensed companies (Appointees), and the remaining one was from the Consumer Council for Water (CCWater).

All Appointees gave their consent to making the modifications to their licence, in some cases after further engagement on the points they made in response to the consultation. We are publishing those responses which made substantive comments alongside this document. All other responses contained only a consent to make changes.

2. Consultation responses and our view

Summary of responses by condition (condition lettering as proposed)

Condition F (Regulatory accounting statements (RAGs))

Two respondents questioned whether the inclusion within new Condition F6 of the obligation to comply with the RAGs will alter the balance of risk for water companies by altering the status of the RAGs from being purely guidance to being a formal part of the regulatory framework. The respondents also sought reassurance that the same level of consultation will be carried out to amend the RAGs as would be required for any Licence amendment.

On the first issue, although the RAGs are called 'guidelines' the previous text of Condition F did require compliance with them where the content of the RAGs related to accounting information, as it does in the new, replacement condition.

On the second issue, paragraph F4 of the new Condition F provides that Ofwat must consult on any change to the RAGs, must have regard to any representations made, and must give reasonable notice (of at least one month) for any amendment to take effect. Where an appointee disputes the revision, paragraph F5 provides for a reference to be made to the Competition and Markets Authority for determination as to whether the revision is appropriate.

After discussion with the companies they accepted the above explanations.

Conditions G (Core customer information)

CCWater stated it was concerned about the removal of the provision making it a requirement for companies and CCWater to meet annually. It argued that the removal of this part of Condition G would remove a valuable failsafe tool for CCWater to ensure that companies are obligated to meet with it at least once a year.

We consider that a healthy working relationship between companies and CCWater is desirable, and that customer interests are best served by a good engagement between CCWater and the regulated companies. However, our view is that holding an annual meeting does not ensure effective engagement. We think this is a redundant obligation as there are broader obligations on Appointees to consult and engage with CCWater both within and outside the licence.

Condition O (termination of appointment)

Two respondents raised a concern that the proposed wording would introduce a substantive change in risk because a replacement appointment could be made immediately after notice was given, thereby limiting their ability to secure terms for transfer of the undertaking to an incoming appointee. This is because we changed the formulation from;

- The Secretary of State has given at least 25 years' notice and that period of notice has expired,
to;
- The Secretary of State has given at least 25 years' notice and the replacement appointment is to come into effect on the expiry of that notice.

In practice, we would only make a replacement appointment once we were satisfied that the necessary transfer arrangements were in place. If we were to do otherwise, it would be difficult to ensure that the company continued to be incentivised to deliver services to customers during that 25 year period and continued investing in the improvement and maintenance of the infrastructure.

The closest equivalent experience we can draw on is the appointment of new appointees, replacing existing companies. In these circumstances transfer schemes must be approved by us or the Secretary of State and in practice this happens on the same day as the grant of the new appointment. We also do not grant new or replacement appointments on a speculative basis, only once all the necessary operational and contractual requirements for delivery are in place.

The existing Appointee would also be consulted. There is an obligation on the Secretary of State to consult prior to making a replacement appointment in section 8 of the WIA91 and a company that applies to become a replacement undertaker must similarly serve notice on the undertaker it is seeking to replace within 14 days of making that application.

After discussing how Condition O is likely to operate in practice and the protections already in place, the two companies consented to the change.

Condition Q (drought payments)

One respondent said that the recent review of the Guaranteed Standards Scheme (GSS) payments¹ meant that compensation payments might increase. They expected that we would amend Condition Q so that there was consistency with the outcomes of the GSS review.

However, this licence simplification exercise is not intended to make substantive policy changes with significant financial implications². We have not, therefore made those changes to the licence condition.

Overall changes to the original licence conditions

Applying the conditions to New Appointees

One Appointee pointed out that the different structure of licences for New Appointees meant it would be preferable to define 'Infrastructure Charge' so that it did not cross-refer to Condition C. As New Appointees do not have condition C in their licences we deleted paragraph E2.1, which refers to it.

Other comments made

No substantive comments were made about the drafting of Conditions A, D, E, H, I, J, M, N, R1, R2.

One respondent urged Ofwat to go further by removing Conditions J (Standards of service) and L (Underground asset management plans) from the licence in their entirety. We agree that there is scope for modernising Conditions J and L or removing them from licences. We intend to address this issue in a future exercise, perhaps as part of a wider review of the controls needed in the licence and elsewhere about standards of service and asset management, so that an appropriate set of checks and balances remains in place.

¹ Since the licence simplification consultation closed, this has now been published as "[Guaranteed Standards Scheme - Recommended changes to the UK Government](#)" and [Guaranteed Standards Scheme: Recommended changes to the Welsh Government](#),

² Our review of the GSS suggested that further evidence was needed before a recommendation could be made about extending the scope of the GSS in relation to extreme weather.

Another respondent raised the possibility of deleting conditions R4 (Stapling condition) and R5 (Customer protection condition) that ceased to apply from the date on which the Appointee exited from the retail market. As these conditions are redundant where the Appointee has exited from the retail market, we have removed these conditions where appropriate.

3. Next steps

We amended the companies' licences on **17 December 2018**, with most of the conditions coming into effect **on 1 January 2019**. Conditions F and N will come into effect on **1 March 2019**, in order to align with the activity required to raise fees for the next and subsequent charging years, without disturbing the arrangements in the current year.

We published our [Consultation on strengthening the regulatory ring-fencing framework](#) on 20 November, requesting comments by 8 January 2019, which proposed bringing the ring fencing requirements in all licences up to the industry-leading standard. For some companies our proposals would result in taking provisions found in current Conditions K and P, and in new Condition I, and combining them in a new updated Condition P with updated definitions in Condition A.

In our consultation "[Proposed modification to simplify various conditions of all undertakers' licences](#)" we indicated that we would modify Condition D for companies operating wholly or mainly in Wales once a new charging regime for developer services was in place in Wales. That process is under way, and we are consulting on the approach to be taken in another consultation entitled "[New connections charges for Welsh companies – consultation](#)". This closes on Thursday 24 January 2019, and if we decide to implement the preferred approach, we will modify Condition D in the way we consulted upon.

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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