

December 2018

Trust in water

## **Retail Exit Code – Non-price protections**

## About this document

The Retail Exit Code (**REC**) was put in place as a transitional arrangement to provide protection to business customers until competition in the retail market becomes fully functional. It is designed to provide default protection to customers who have not actively selected their water supplier in areas where the incumbent has exited the market.

In this document we are consulting on strengthening the REC to ensure that customers who are on deemed contracts (i.e. they have not otherwise negotiated and agreed a contract with their retailer) are protected against non-voluntary changes to their non-price terms<sup>1</sup>.

As we consider that these changes could mean that customers are worse off than they were pre-market opening, we are proposing to modify the REC to introduce an explicit '**no worse-off**' principle with respect to the non-price terms. We consider that this is in line with the original intent and spirit of the REC and would prevent retailers from making any non-voluntary changes to their non-price terms which could lead to customers being worse off.

While our primary objective in seeking to modify the REC is to strengthen customer protections, it is not our intention to ossify existing arrangements by stifling innovation or preventing retailers from making efficiency enhancing changes that may actually benefit customers. For this reason, we consider that when interpreting the "no worse off" principle, retailers should be able to alter the non-price terms and conditions for customers on deemed contracts, if they are: transparent about any proposed changes; are able to clearly articulate what the impact on individual customers will be and are able to demonstrate to customers why, and how, customers will be at least "no worse off" as a result of those changes.

While this is currently our preferred approach, we remain open-minded. By launching this consultation, therefore, we are seeking stakeholders' views on the nature of the harm that customers may experience as a result of non-voluntary changes to their non-price terms; to identify and assess any other options that may be open to us to ensure that customers who do not engage in the market are adequately protected;

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<sup>1</sup> We are also consulting separately on the [price protections contained in the REC](#).

and to investigate the potential risks or un-intended consequences of any proposed changes.

We will take account of the feedback from stakeholders during this consultation exercise before making a final decision. We anticipate that we will issue a decision document in the second quarter of 2019 which, if appropriate, will also include the modified REC.

## Responding to this consultation

We welcome your responses to this consultation by close of business on 15 February, 2019.

You can email your responses to [retailexitcode@ofwat.gsi.gov.uk](mailto:retailexitcode@ofwat.gsi.gov.uk). You can submit your responses by post to:

Retail Exit Code  
Ofwat  
Centre City Tower  
7 Hill Street  
Birmingham  
B5 4UA

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 2018 and the Environment Information Regulations 2004.

If you would like the information you have provided to be treated as confidential, please be aware that, under the FoIA, there is a statutory ‘Code of Practice’ with which public authorities must comply and 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, in itself, be regarded as binding on Ofwat.

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## 1. Background

### 1.1 Protecting customers in the business retail market

Ofwat has a statutory duty to protect customers where appropriate by promoting effective competition<sup>2</sup>. As a regulator, we also have a vision that water and wastewater customers should have trust and confidence in the services they receive.

The business retail market in England opened to competition in April 2017<sup>3</sup> and means that all business customers are now free to choose the retailer of their water or wastewater service for the first time.

One way to protect customers in this market is to make sure that the market arrangements are effective, with high levels of competition and innovation among retailers to win and retain customers, as well as minimising any unnecessary or onerous burdens on retailers and removing any undue barriers to entry and expansion. Effective competition means that customers have the freedom to switch to a retailer that offers them a service that better suits their specific needs, at the best possible price, or to negotiate a better deal with their existing retailer.

Customers have already begun to take advantage of opportunities in the new market – in the first year, around 10% engaged in the market by switching, renegotiating, or considering switching<sup>4</sup>. Making this process as simple and easy as possible is extremely important to help ensure that customers have the incentive and the ability to engage in the market. We are working with the sector to address and remove a number of frictions which have been identified in the market to make sure that it works more effectively. We expect this to help more and more businesses to take advantage of the choices they now have by either switching to a new retailer, or renegotiating terms with their existing retailer, if they are unhappy with the service they receive.

While competition can be an incredibly powerful mechanism to drive improvements for customers, we also recognise that some customers, particularly smaller

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<sup>2</sup> [Water Industry Act 1991, Section 2.](#)

<sup>3</sup> In Wales, the water supply and sewerage market is open to competition for customers using more than 50ML but not customers using below this threshold. This reflects the policy position of the Welsh Government

<sup>4</sup> See [Open for business: Reviewing the first year of the business retail water market.](#)

customers, may be reluctant to engage in the market for a range of different reasons. It is important that such customers are protected while the market develops.

Such customer protection measures are an important part of a well-functioning market, but it is also important to ensure that they do not stifle innovation, hamper the development of effective competition or restrict the ability of customers to secure a deal that best suits their specific requirements.

This consultation considers protection on non-price contract terms. We are also consulting separately on the price protections contained in the REC.

## **1.2 The Retail Exit Code (REC) – ensuring that customers are ‘no worse off’**

When the market was opened to competition, many incumbent water companies who had previously served retail business customers in their area of appointment chose to exit the market. Before doing so, however, the regulations governing this process (generally referred to as the Exit Regulations) require the incumbent to apply to the Department for Environment, Food and Rural Affairs (**Defra**) for permission to transfer all its business customers in its area (**the exit area**) to one or more other retailers that hold a Water Supply and Sewerage Licence (**WSSL**)<sup>5</sup>. The company to whom the customers are transferred is referred to as an Acquiring Licensee and can be either an associated WSSL retailer (i.e. part of the same overall company), or an unrelated WSSL retailer. These companies can offer retail services across the whole business market.

Under the Exit Regulations, all licensees providing, or proposing to provide, business retail services in an exit area are required to make and keep under review a Scheme of Terms and Conditions that will apply in cases where affected customers<sup>6</sup> have not otherwise negotiated and agreed a contract (this is referred to as a deemed contract

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<sup>5</sup> Chapter 4 of the Water Act 2014 (the Act) gives the Secretary of State the power to make regulations to provide for retail exit – that is, for an appointed water or sewerage company to transfer all of its business customers to one or more holders of a WSSL (the acquiring licensee).

<sup>6</sup> In addition to transferred customers, this also includes certain other eligible customers in the exit area e.g. new customers; customers who request Ofwat to direct another WSSL retailer to take over supply; and customers receiving interim supply

or a default contract).<sup>7</sup> In addition, Ofwat is required to issue a code setting out the basis for the schemes produced - including both price and non-price requirements - and the various principles with which these schemes must comply. This is referred to as the Retail Exit Code (**REC**).<sup>8</sup>

In developing the REC, our aim was to ensure that customers on deemed contracts are generally '**no worse off**' as a result of being transferred to an acquiring licensee. While it does not currently refer expressly to ensuring that customers are '**no worse-off**', it is clear from the Exit Regulations (and previous Ofwat consultations on the REC) that this is what is broadly intended.<sup>9</sup>

The Explanatory Memorandum which accompanied the publication of the Exit Regulations, for example, notes that the regulations are intended "to ensure that customers in exit areas are never left without a licensee and provide customer protections that are broadly equivalent to those they would have been provided if the undertaker had not exited the market".<sup>10</sup>

It also explains that in enabling companies to exit the market "the Government wants to ensure that the customers of an exiting undertaker have access to the same standards of protection that they would have had if they had remained with the undertaker<sup>11</sup>."

Furthermore, the Memorandum goes on to note that the Regulations are designed to minimise disruption to transferred customers and "help ensure that they are made no worse off as the result of the exit"<sup>12</sup>.

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<sup>7</sup> Regulation 29 of the Exit Regulations, available at <https://www.legislation.gov.uk/ukxi/2016/744/contents/made>

<sup>8</sup> Ibid, Regulation 30 of the Exit Regulations.

<sup>9</sup> This intention is referred to in the government's explanatory memorandum to the Exit Regulations and in Ofwat's Consultation and Conclusion documents in designing the Retail Exit Code. See, The Water and Sewerage Undertakers (Exit from Non-Household Retail Market) Regulations 2016, Explanatory Memorandum, 10.3,

[https://www.legislation.gov.uk/ukxi/2016/744/pdfs/ukxiem\\_20160744\\_en.pdf](https://www.legislation.gov.uk/ukxi/2016/744/pdfs/ukxiem_20160744_en.pdf);

Customer protection for the non-household retail market: deemed contracts – a consultation, p22, [https://www.ofwat.gov.uk/wp-content/uploads/2015/10/pap\\_con20151030deemedcontract.pdf](https://www.ofwat.gov.uk/wp-content/uploads/2015/10/pap_con20151030deemedcontract.pdf); and Consultation on retail exit code: conclusions, p10 [https://www.ofwat.gov.uk/wp-content/uploads/2016/02/pap\\_tec20160406reconconc.pdf](https://www.ofwat.gov.uk/wp-content/uploads/2016/02/pap_tec20160406reconconc.pdf)

<sup>10</sup> The Water and Sewerage Undertakers (Exit from Non-Household Retail Market) Regulations 2016, Explanatory Memorandum, paragraph 2.2.

<sup>11</sup> Ibid, paragraph 7.3

<sup>12</sup> Reference to Section 29(7) of the Exit Regulations.



While we consider that this is the broad intent of the REC, we are concerned that in practice it does not appear to provide sufficient protection for customers on deemed contracts against non-voluntary changes in their **non-price terms**<sup>13</sup>, and this may lead to customers being worse off than they were before market exit. To minimise the risk of customer detriment, therefore, we consider that a modification to the REC may be necessary.

### 1.3 Our consultation

We are consulting on a proposal to introduce an explicit '**no worse off**' principle into the REC to strengthen protection for customers on deemed contracts against non-voluntary changes in their non-price terms. This is intended to minimise the risk of customers suffering harm as a result of changes to the non-price elements of their contract. We consider that this is in line with the original intent and spirit of the REC.

At the same time, however, it is not our intention to stifle innovation or prevent retailers from introducing changes to their non-price terms that may ultimately benefit customers. For this reason, we are proposing that the “no worse off” principle would enable retailers to alter the non-price terms and conditions for customers on deemed contracts, but only if they are transparent about these proposed changes and are able to demonstrate to customers why, and how, these will not make them “worse off overall”.

Although a modification to the REC on the basis outlined above is currently our preferred approach, we remain open-minded about the options available to us, including the option to “do nothing”.

By launching this consultation, we are seeking stakeholders' views on the nature of the harm that customers may experience as a result of non-voluntary changes to

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<sup>13</sup> In relation to non-price requirements, the REC sets out a number of principles with which acquiring licensees must comply in making a Scheme of Terms and Conditions. In general, these require acquiring licensees to continue to provide retail services in a retail exit area and also to ensure that non-price terms included in a Scheme of Terms and Conditions are consistent with its licence obligations. The REC does not refer to specific non-price terms. However, in previous consultations we have also highlighted areas such as transparency of terms, termination of the contract, duration of the contract, notice periods, disconnection and relocation, billing frequency, back billing etc. See for example, [Customer protection for the non-household retail market: deemed contracts – a consultation](#) and [Consultation on retail exit code: conclusions](#).

their non-price terms; to identify and assess any other options that may be open to us to minimise the risk of customer harm and ensure that customers who have not yet engaged in the market are adequately protected; and to investigate the potential risks or unintended consequences of any proposed changes.

We will take account of the feedback received from stakeholders as a result of this consultation exercise to inform our decision on next steps.

## 2. The case for change

### 2.1 Our concerns

As explained above, our primary concern is one of customer protection and ensuring that those customers on deemed contracts are not at risk of being made worse off as a result of the new market arrangements while the market develops. By definition, these customers have not actively negotiated or agreed terms and conditions with their retailer. We do not consider it reasonable for retailers to take advantage (either intentionally or unintentionally) of this lack of engagement by imposing a change in their non-price terms that mean that customers are worse off than they were before market exit.

The non-price terms encompass a range of different elements, but the need for this review has been prompted by complaints from customers about non-voluntary changes to their billing arrangements. It is important to stress, however, that while we use the specific example of billing throughout this document to illustrate the nature of our concerns, we believe the principle is much wider than this and relates generally to the fair treatment of customers who have not yet engaged in the market.

### 2.2 The potential for customer detriment – the example of customers' billing arrangements.

As we have explained above, we consider that the intention of the provisions in the Exit Regulations and the REC is to ensure that customers are `no worse off` as a result of the new market arrangements. Indeed, the Exit Regulations include a specific reference to billing as they stipulate that “an acquiring licensee’s scheme under this regulation must provide for each transferred customer to be billed by the same method, and pay by the same method, as immediately before the exit date.”<sup>14</sup>

Over the last number of months, however, we have observed that some customers have had their billing arrangements changed from a situation where they had previously been billed in arrears to now being billed, wholly or partially, in advance. This has already resulted in a significant number of complaints to Ofwat and CCWater. The nature of the complaints received indicates that for many customers,

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<sup>14</sup> Regulation 29(7).

this change was unexpected and unwelcome. In some instances, customers had either not been aware that their terms were being changed, or when they did become aware, felt that they were not given sufficient information about its potential impact. Many also felt that they had not been given any choice and would have preferred to retain their existing billing arrangements. In many instances, customers were frustrated that they were being asked to pay in advance for water that they had not yet consumed and felt that this was unfair.

At the outset, it is important to note that our concern is not about advance billing **per se** as many types of services are billed in this way and many customers, including unmetered customers<sup>15</sup>, may have already been billed in advance prior to market exit and may prefer this arrangement.

Similarly, we are not concerned about situations where customers have made an active and informed choice over the relevant parts of their contracts and, therefore, have **voluntarily** entered into contracts where some form of advance billing is part of the terms. (As these customers have actively agreed contract terms, they would not be covered by the REC).

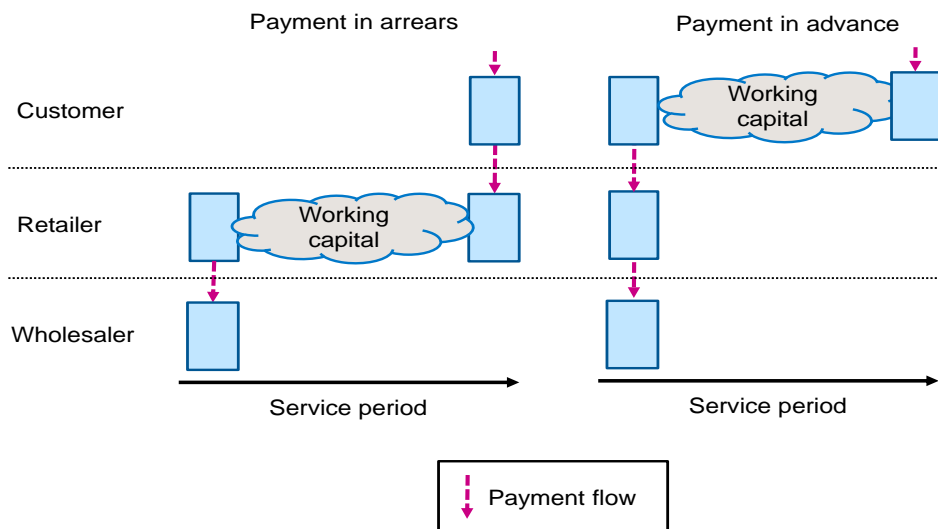
We are concerned, however, about customers who have not actively chosen this arrangement and have had a non-voluntary change in their non-price terms imposed upon them. While it is not clear that the specific billing provision in the Exit Regulations covers the circumstances described above (e.g. some retailers have interpreted the provisions as referring to the method of billing i.e. paper or electronic), in our view, this can harm customers and lead to them being worse off than they were prior to market exit. It is therefore not in keeping with the spirit of the REC.

### **The nature of customer detriment – direct impacts**

By moving customers to advance billing, retailers are effectively transferring some of their working capital costs to customers as they now need to ensure that they have sufficient funds in place to enable them to pay their bill at an earlier date. A stylised illustration of this is given in Figure 1.

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<sup>15</sup> It is standard industry practice, for example, for unmetered customers to be billed in advance since their bills are based on the rateable value of their property. These customers may therefore be in the same situation following their transfer to a new retailer.

**Figure 1** Stylised illustration of billing cycles

Source: Ofwat

This will have a direct financial implication for these customers as, although the nominal bill may remain the same, these customers now face either a direct cost if they have to use credit to pay the advance bill, or incur an opportunity cost if they pay the bill out of cash flow. The cost is equal to the customer's nominal cost of capital. For example, for a customer with a water bill of £500 per year and a nominal cost of capital of 10%, the financial cost of paying one year in advance as opposed to in arrears is £50 per year (i.e. £500 \* 10%).

In addition to the direct and ongoing financial costs incurred by customers, there are also likely to be some transitional and operational costs to businesses from adjusting to the new payment cycle. This is likely to be particularly significant for small and medium sized businesses for whom the impact on cash-flow and the challenge of raising working capital to pay an annual or biannual water bill may be material.

The nature of the complaints relating to advance billing suggest that for many customers, the change to their billing arrangements came as a surprise. We understand, however, that in some instances retailers have taken steps to inform customers about the changes and have also sought to encourage customers to agree to move to monthly direct debit payments to spread out the costs and offered them a financial incentive to do so.

These financial incentives could help to offset the potential costs to customers if they have agreed to move from their previous billing in arrears arrangement, and could mean that they are no worse off overall.

We would be concerned, however, if customers who have not actively chosen to move to direct debit payment were then defaulted onto other advance billing arrangements that make them worse off compared with their existing billing arrangements.

### **Customer detriment – barriers to the effective functioning of the market**

In addition to the direct impact on customers, it would appear that in some instances non-voluntary changes to customers' non-price terms have the potential to act as a barrier to switching and can impact adversely on the incentive and ability of customers to engage in the market. (Again, it is important to stress that whilst we use the example of advance billing to illustrate a particular concern that we have identified, the principle is wider than this).

While the market rules allow a retailer to object to a request from a customer to transfer to a new retailer if that customer has not paid an outstanding debt,<sup>16</sup> we have been told that in some instances, the non-payment of an advance bill may have been treated as an outstanding debt and used a reason to block a customer's transfer request.

For the avoidance of doubt, for customers on deemed contracts, we do not think it is appropriate for a retailer to use failure to pay an advance bill for services that have not yet been consumed as a reason to block the transfer of a customer to a new retailer. As these are by definition customers who have not engaged in the market so far, this has the potential to create an additional obstacle or barrier if, and when, they do try to engage.

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<sup>16</sup> MOSL. Wholesale Contract Schedule 1: Part 1: Objectives, Principles and Definitions, Version 2.0, page 37, 38.

## **2.3 Facilitating the development of effective competition - the need for a balanced approach**

As we have highlighted above, our primary objective in considering a change to the REC is to strengthen the protection for customers who have not engaged in the market. At the same time, however, it is also important to ensure that the market develops effectively and that retailers are able to drive change and innovation that will ultimately benefit customers.

As we have also explained, we recognise that in a competitive market, customers are able to switch if they are not happy with terms or service being offered by retailers. Nevertheless, given that competition is still developing (and the fact that some customers, particularly smaller customers, may have fewer options for switching at this time), we need to strike an appropriate balance between enabling innovation and dynamic efficiency in retailing but also ensuring that disengaged customers are adequately protected.

We understand that some retailers may consider that an ability to change default terms and conditions may be necessary and proportionate to enable them to compete effectively in the market and may be in consumers' interests.

From a retailer perspective, for example, there may be strong commercial incentives to introduce changes to customers' non-price terms e.g. to rationalise terms, reduce administrative costs or improve cash-flow. These efficiencies could, in turn, allow a retailer to improve other aspects of its offer to customers. As a result, customers may be no worse off overall.

However, as these are "default" terms and conditions which have not been actively negotiated and agreed by the customer, the onus must be on the retailer to clearly communicate any proposed change to their customers; to explain why they are introducing the changes; what the impact on individual customers will be and why, as a result of these changes, customers will, on balance, be no worse off.

## 3. Policy options

### 3.1 Our policy objectives

As we have explained previously, Ofwat has a statutory duty to protect customers, where appropriate by promoting effective competition. This duty also informs our objectives for the functioning of the business retail market<sup>17</sup> and, therefore, our assessment of whether, and how, we need to take action to address the concerns highlighted in Section 2. These are summarised below:

- **Consumer protection** – We seek to ensure that there are proportionate mechanisms in place that protect customers who have not yet engaged in the market in the event that they are, or could be, harmed by their lack of engagement. We therefore define this objective as meaning that we want to ensure that customers are protected from non-voluntary changes to their non-price terms which can mean that they are worse off than they were pre-market exit.
- **Promoting competition** – Competition can benefit customers by placing downward pressure on prices, providing greater choice, increasing quality and spurring innovation. We need to consider the extent to which changes in the regulations of non-price terms may impact on competition – bearing in mind that our focus is on ensuring that competition works in the interests of customers and not the promotion/protection of individual competitors.

In addition, in considering the various policy options open to us, we also strive to achieve the following general objectives<sup>18</sup>:

- **Simplicity** – The simpler the protection, the greater the clarity and certainty for retailers and retail customers. This includes ensuring a correct and consistent interpretation of the protections across relevant retailers reducing regulatory burden.

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<sup>17</sup> Customer protection for the retail market: proposal to the Secretary of State and Welsh Ministers for regulations in connection with standards of performance for the supply of water and the provision of sewerage services, available at <https://www.ofwat.gov.uk/publication/customer-protection-retailmarket-proposal-secretary-state-welsh-ministers-regulations-connection-standards-performancesupply-water-provision/>

<sup>18</sup> These were consulted on, and broadly accepted, as part of a [previous consultation](#) on the REC.



- **Proportionality** - The direct costs of implementing the intervention should be proportionate to the benefits gained from the intervention.

Where possible, we intend for the regulatory arrangements to fulfil as many of these objectives as possible. However, we recognise that at times, but not always, these objectives may be at odds with each other.

Where objectives are at odds with each other, we may have to balance the conflicting objectives. The appropriate trade-off might differ for different groups of customers. In particular, we note that the UK Government's strategic priorities for Ofwat require us to 'promote an enhanced focus by water companies on the needs of small business customers that may struggle to access the best deals'.<sup>19</sup>

## 3.2 Policy options

In general we consider that there are a number of broad options available to us:

1. Do nothing;
2. Require retailers to be open and transparent about any proposed change in non-price terms;
3. Ban specific changes to specific non-price terms (e.g. a move to advance billing) for customers on deemed contracts;
4. Introduce an explicit 'no worse off' principle into the REC.

### Option 1: Do nothing

One option would be to decide that intervention is not necessary or appropriate at this stage and let the market develop.

As we have noted previously, we are encouraged by the progress we have seen to date in market development, particularly for larger customers. We expect more and more businesses to take advantage of the choices they now have as the market develops further and to switch retailer if they are unhappy with the service they receive or with the terms and conditions they are offered. However, we also

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<sup>19</sup> DEFRA (2017), 'The government's strategic priorities and objectives for Ofwat', p9, [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/661803/sps-ofwat-2017.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/661803/sps-ofwat-2017.pdf)

recognise (from our review of the new retail market and the experience of other regulated utility markets) that some customers, particularly smaller customers, may be reluctant to, or find it difficult to, engage in the market.

If we do nothing, therefore, we may see more retailers introducing changes to the non-price terms contained in their deemed contracts which make customers worse off than they were pre-market exit. In the case of billing, for example, in the short term at least, it is likely that more retailers would move customers onto arrangements which involve some form of advance billing. While this could help to reduce retailers' costs and improve their overall financial viability, customer harm could increase significantly.

In the longer term, it is expected that competition will continue to drive improvements and help to ensure that retailers' non-price terms more closely align with customers' preferences. In the meantime, however, the risk remains that customers who have not engaged in the market and remain on deemed contracts, are vulnerable to non-voluntary changes in their non-price terms being imposed upon them which leave them worse off.

Where we have concerns that customers may be suffering detriment now, or are at risk of suffering ongoing detriment, we need to do something about it. In our view, therefore, a "do nothing" option is not compatible with our duty to protect customers and it also risks damaging trust and confidence in the sector since some customers will have found themselves worse off since market exit.

### **Option 2: Require retailers to be transparent about any proposed change in non-price terms**

In an effort to encourage customers to engage in the market, another option would be to strengthen the transparency requirements on retailers to improve disclosure of information and ensure that customers are able to make an informed choice.

This could be achieved either via a modification to the Customer Protection Customer Code of Practice (**CPCoP**)<sup>20</sup> or through a modification of the REC<sup>21</sup>.

Under this option, we could require retailers to clearly inform customers about any proposed change in their non-price terms; to explain the potential impact that this change might have on customers relative to their existing terms and, to inform them of their options if they are not happy with the proposed change e.g. change to another deal with the retailer or switch to another retailer.

While this should help to facilitate customer engagement, we recognise, however, that as the market is still developing, greater disclosure on its own is unlikely to provide sufficient protection for customers who are unwilling or unable to shop around.

### **Option 3: Ban changes to specific non-price terms and conditions for customers on deemed contracts**

A further option would be to prohibit any, or specified, changes to non-price terms for customers on deemed contracts. This could be achieved either via a modification to the CPCoP or through a modification of the REC.

We could, for example, seek to prohibit retailers from changing the billing terms for customers on deemed contracts. This would capture the situation outlined previously and prevent customers who had previously been billed in arrears from being moved, on a non-voluntary basis, to an arrangement which meant that they were billed wholly, or partially, in advance.

This option has a number of attractions. Not only could it directly address the concerns that have been raised with us in relation to advance billing, it would also be relatively simple to understand and enforce.

On the other hand, however, while it may prevent retailers from changing the specified non-price terms (which would also need to be very carefully defined), it

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<sup>20</sup> Ofwat is able to propose a change to the CPCoP at any time by consulting with the affected retailers and anyone else we consider appropriate. We would then need to consider the responses and decide whether to accept, reject or amend the proposed change. Having done so, we would then consult on that decision for a minimum of 28 days.

<sup>21</sup> The REC includes requirements on the provision of information to customers who have been transferred to an acquiring licensee.

would still leave open the possibility of retailers making other changes to their non-price terms that might make customers worse off. In addition, there is also a risk that an outright prohibition could ossify existing arrangements and limit the ability of retailers to innovate or make efficiency enhancing changes that could lead to customers being better off.

**Option 4: Modify the REC to insert a general principle that consumers on deemed contracts must be “no worse off”**

A further option, and our preferred approach, would involve the introduction of a general ‘**no worse off**’ principle into the REC to strengthen protection for customers on deemed contracts against non-voluntary changes in their non-price terms. This would not only address the immediate concerns identified as a result of changes to customers’ billing arrangements but would also ensure that customers were protected against other changes in non-price terms that could make them worse off.

We consider that this is broadly in line with the original intent and spirit of the Exit Regulations and the REC. It also removes any ambiguity that may exist about our expectations of the way that retailers should treat customers on deemed contracts.

While our primary objective in seeking to modify the REC is to strengthen customer protections, it is not our intention to ossify existing arrangements, stifle innovation or prevent retailers from making efficiency enhancing changes that may actually benefit customers.

For this reason, we consider that when interpreting the “no worse off” principle, a more pragmatic approach may be appropriate. This would enable retailers to alter the non-price terms and conditions for customers on deemed contracts, but only if they are transparent about any proposed changes; are able to clearly articulate what the impact on individual customers will be and are able to demonstrate to customers (and if challenged by Ofwat) why, and how, customers will be at least “no worse off”<sup>22</sup> as a result of those changes.

We consider that this option helps to meet our objective of protecting the interests of customers, wherever appropriate by promoting effective competition. We recognise, however, that a principle-based approach may not be as simple in terms of ease of understanding as an outright ban. We also recognise that in terms of enforcement,

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<sup>22</sup> See section 3.2.6 of the draft Retail Exit Code.

subsequent assessment against the principle may be more complex. However, as we have stressed above, the onus is firmly on the retailer to be able to provide evidence to demonstrate to its customers, and Ofwat, that it is complying with the 'no worse off' principle.

We expect retailers to be able to demonstrate with a reasonable level of accuracy that their full range of customer groups (e.g. by volume, billing method or other characteristics) are no worse off than they were before market exit<sup>23</sup>. We would be very concerned if we found that this approach was being used by retailers to introduce changes that resulted in significant numbers of customers, or particular groups of customers, being worse off. We also expect retailers to be open and transparent with consumers about the changes and the impact of them.

In terms of implementation, we recognise that some retailers may have already made changes to their terms and conditions for customers on deemed contracts. This could mean that, once implemented, they may not be compliant with the modified REC. It is not our intention to take retrospective action or to use any new rules to penalise past behaviour which had been legitimate in the past.

In the event that we change the REC to include the modification outlined above, we would expect all retailers to comply with the new rules **going forwards**. It may be necessary, therefore, to include a transitional period within the REC modification to allow licensees to amend their processes and become compliant with the amended REC<sup>24</sup>.

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<sup>23</sup> See section 3.2.7 of the draft REC.

<sup>24</sup> Section 3.2.8 of the draft REC.

## 4. Request for stakeholder input and next steps

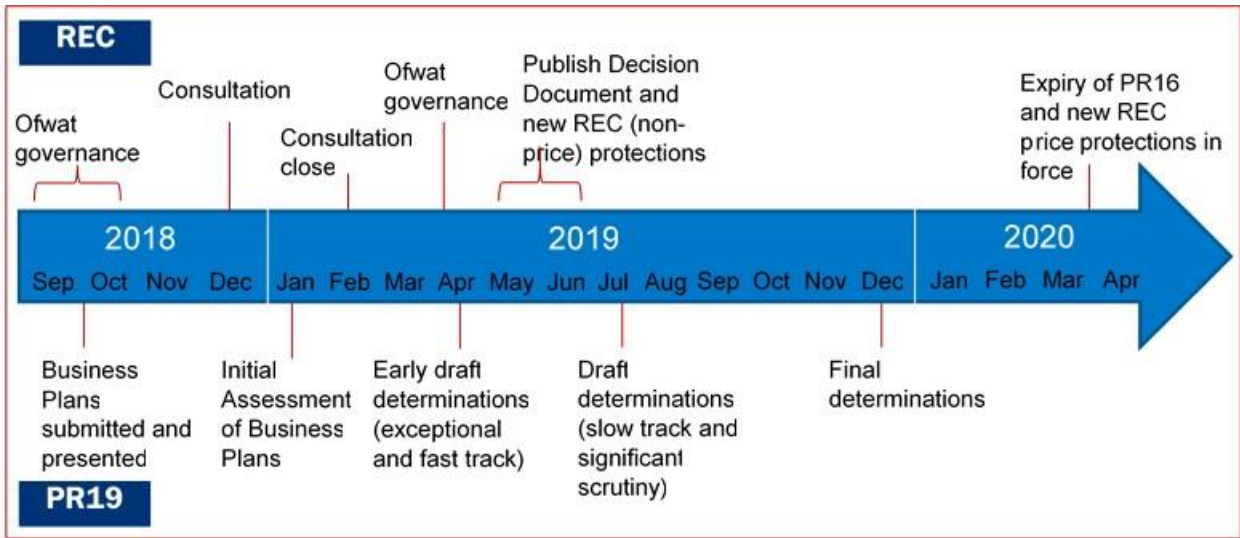
As we have highlighted above, we consider that action is needed to ensure that customers on deemed contracts are not worse off as a result of non-voluntary changes in their non-price terms. We have also explained why we think a modification to the REC to include a “no worse off” principle is the most appropriate mechanism to ensure that customers are protected.

Nevertheless, we remain open-minded and will take account of the views of stakeholders before reaching a final decision. We are keen, therefore, to hear from stakeholders, with supporting evidence where possible, about:

- the nature of the harm that customers on deemed contracts may experience as a result of non-voluntary changes to their non-price terms and whether you agree that action is needed to strengthen their protection;
- the policy options set out in this document and their impact not only on customers but on individual retailers;
- whether our preferred option strikes an appropriate balance between protecting customers who have not yet engaged in the market and also allowing retailers to innovate or improve efficiency.

Once we have had an opportunity to consider the responses to this consultation, we will issue a decision document and, if appropriate, this will be accompanied by the publication of a revised REC.

As we are also consulting separately on the price protections contained in the REC, we set out a provisional timetable for both consultations below. This also shows some key PR19 milestones as these may be relevant for our decisions on the price protections.



## **5. Appendix 1: Proposed draft revised REC.**

Our proposed [draft revised REC](#) is available here.



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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