Sutton & East Surrey Water Services Limited, trading as SES Business Water

Retail Exit Code: Proposals for price protections beyond March 2020

Q1. Do you agree with our proposal to remove the distinction between transferred and otherwise eligible customers in the REC?

We agree with your proposal. We do not see any market data or customer benefit of maintaining the distinction.

Q2 Do you agree with our proposal to remove the distinction between SME's and non-SME's in the REC?

We concur that there is an inherent difficulty of understanding an organisations employee numbers and that this is not a good proxy for the sophistication of customers or their water consumption. Therefore, we see no material benefit to customers or the market in maintaining the distinction.

Q3 Do you agree with our proposal to split the current 0-5 ml band into 0-0.5 ml and 0.5 – 5 ml?

We understand the rationale underlying this split in terms of customer awareness / engagement based on market switching and the research undertaken. If there is to be a differential approach to price control within the 0-5 ml band then we agree with the split. However, please refer to our response to question 4.

Q4 Do you agree with our proposal to retain a net margin approach to the protections for these customers?

We do not agree with a net margin approach being maintained for 0-0.5 ml customers, indeed we believe that in taking this approach OFWAT could miss a significant opportunity to enhance awareness and engagement in this segment of the market.

Whilst we recognise the current levels of awareness and engagement are a below other areas of the market, we believe that this is driven by the low levels of margins available in this segment. Current levels are effectively acting as a deterrent.

1. Retailer customer acquisition costs cannot be recovered within reasonable expectation of a customer's lifetime value.
2. TPI's involvement has been a significant factor in driving engagement for larger consumers but the margins available are not sufficient to enable a return on their acquisition costs for smaller customers, even when water procurement is promoted alongside energy or other utilities.
3. Customer savings are not sufficient to motivate consumers to switch even if they engage with the market.

In our view 'margin drives the behaviours' for all parties. If more margin is available to enable better customer savings and sufficient recovery of acquisition costs then momentum will be generated. This will raise awareness and result in greater engagement.

We understand that this is supported by experience in the Scottish market.

Therefore, we believe the time is now to take a bold step and give true competition a chance. Whilst wholesale costs are yet to be finalised for the period there is expectation of wholesale price reductions. These reductions can be used to fund a greater margin whilst mitigating price increases for customers. This is an opportunity that may not exist in the future.

The current proposals will in our opinion simply maintain the deterrent. No margin will simply mean no movement in the market.

Q5 Do you agree with our proposal for a one-off adjustment for the 0-0.5 ml usage band? Do you agree with the level of this proposed adjustment?

The movement is welcomed. However, we do not consider it to be significant enough to provide for the costs that were excluded from the original retail margin calculations such as MOSL costs, working capital, and increased meter reading.

Q6 Do you agree with our proposal for ongoing adjustments for the 0-0.5 ml usage band?

If the one-off adjustment were sufficient then in principle we would be in agreement with the proposal.

However, we believe this should be subject to there being no statutory or regulatory intervention in the market which impacts retailers cost bases, or that should they occur, that further one-off adjustments be allowable to recover costs incurred.

Q7 Do you agree with our proposal to move to a gross margin cap for the 0.5-5 ml customers?

Yes we agree with the proposal to remove individually specified regional projections. The gross margin cap approach will simplify comparisons with alternative product options offered by retailers which have the wholesale plus management fee structures on a national basis.

Q8 Do you agree with our proposal for the level of the gross margin cap for 0.5-5 ml customers?

As is recognised within the proposal, given that the outcomes of PR19 are not yet known, it is not possible to calculate the true impact.

The methodology of adjustments are calculated on a £ per customer basis but income is reliant upon an uncertain wholesale cost which creates the risk that the intended outcomes are not realised. Therefore, whilst the headline adjustment calculated equates to a 2% increase that could be completely eroded.

Therefore, it is in our opinion the actual % should be adjusted based on PR19 outcomes.

We also find it in principle difficult to reconcile why percentage margins in wastewater should be higher than for water. When considering the core functions of a retailer of meter reading, billing and customer service, meter reading costs are a fixed cost incurred in water, whilst a retailer providing a single waste service does not incur meter reading costs and the other functions are often undertaken together. Given that in our view average per SPID market retail bills are higher for waste than for water in the 0.5-50ml segment, we believe water percentage margins should be higher than those for wastewater.

Q9 Do you agree with our proposal not to make ongoing adjustments for the 0.5-5 ml usage band?

We do not agree that such a commitment should be made give the current uncertainty of outturn wholesale costs.

Q10 Do you agree with our proposal for the 5-50 ml band?

We agree with the principle of alignment with the 0.5-5 ml band, subject to our earlier comments.

Q11 Do you agree with our proposal for the >50 ml band?

We support the proposal to remove gross margin controls. This customer group are clearly engaging in the market and effective competition exists to ensure choice.

Q12 Do you agree with our proposal for unmetered customers, assessed customers, trade effluent customers and special agreements?

Please refer to our comments relating to 0-0.5 ml customers.

Q13 Do you believe that the drafting of the proposed revised REC is appropriate, in light of the proposals we have put forward?

In terms of your current proposals we concur with reflecting the REC in the proposed manner

Q14 Do you agree with our approach to non-exited companies and potential future exit?

We agree with your approach, however, given the impending acquisition by Business Stream these provisions are now unlikely to be required.