

Water2business' responses to the Ofwat consultation - review of the REC

- Q1) Noting our key objective for the review, do you agree with our four complementary objectives for the review of REC price and non-price protections? If not, please explain why. Do you consider that any other or different objectives may be appropriate for our review?

W2B: Agree.

- Q2) Do you agree that some form of price protections are still required for Group One and Group Two customers? Please explain your answer, providing supporting evidence wherever possible.

W2B: We believe that price protections for both Group one and Group two customers limit the ability for the market to be competitive. Particularly in Group one, where capping prices retails such a small margin, resulting in engagement and incentive levels remaining stagnant.

- Q3) do you agree that due to both lower levels of awareness, activity and incentives to engage in market and the presence of significant market frictions, price caps for Group One customers should closely reference efficient, forward looking costs of serving such customers?

W2B: No, see response to question 2

- Q4) Do you agree that there is merit in retaining the present form of price cap protections for Group One customers (based on a cost to serve and net margin approach)?

W2B: No, see response to question 2

- Q5) Do you agree that there is merit in retaining the present form of price cap protections for Group Two customers (based on a gross margin approach, with gross margins retained at present levels of 8% for water and 10% for wastewater)?

W2B: No whilst this is marginally better (based on increased margin), the point remains that this is a barrier to competition.

- Q6) Do you agree we should undertake a more detailed, 'bottom up' analysis of the costs – on a forward-looking basis - that an efficient Retailer may incur to serve Group One customers? If not, please explain your preferred approach.

W2B: Should the cap remain for group one customers; the assumed costs do need to be reviewed in a bottom-up analysis as these are outdated and inaccurate.

- Q7) Do you have views concerning the level of the net margin that an efficient Retailer may expect to earn in respect of serving Group One (0-0.5MI) customers?

W2B: The reality of the market and recent independent reviews have confirmed that the majority of retailers run at a loss.

- Q8) Where we undertake a detailed review of efficient, forward looking costs for Group One customers, do you have views about if and how we should take account of forward-looking costs that an efficient Retailer may incur in serving customer Groups Two and Three?

W2B: Our view is that there should be no controls for groups two and three and therefore a review of forward-looking costs would not be required.

- Q9) Do you have views concerning the possible merits and/or risks of moving to redefine Group One customers in terms of 'customer' rather than 'eligible premises'? Please set out the reasons for your views.

W2B: The reality of this suggestion is that there is not sufficient enough data in the market to ever make this achievable or accurate. The cost of implementing this would greatly outweigh any possible benefit, therefore we would not support this redefinition.

- Q10) Do you agree there is merit or scope to specify REC price caps in terms of the six tariff types listed above? How should these be simplified and what are the benefits and costs associated with this?

W2B: Should the price caps remain in place, we do not propose any change to the categories.

- Q11) Do you consider that retail costs to serve a particular customer type or tariff type are likely to vary significantly across different regions in England? Please provide information and evidence to support your answer.

W2B: Yes, the costs of meter reading as an example can vary by as much as over 488% depending on area to simply read a meter.

Below are our biannual meter reading charges as a percentage of our lowest fee.

197%
488%
123%
153%
142%
332%
313%
394%
100%
207%
415%
311%
153%

- Q12) Should Ofwat consider simplifying the retail price caps by removing or reducing the observed variation in allowed costs and/or net margins between regions? Please explain your answer and provide supporting evidence.

W2B: Should the caps remain; these costs should be reviewed as part of the bottom-up analysis to produce a more accurate representation of costs in a particular area. The need for this would be removed if the caps were removed.

- Q13) Do you agree with our proposal to retain the current REC non-price protections? If not, please set out your proposed changes to the current non-price protections, providing supporting evidence where necessary.

W2B: Whilst we agree with the principles noted in 7.4, this approach feels very much “chicken and egg” i.e., the protections are in place because of a stagnant marketplace, whilst you could also say the marketplace is stagnant because of the protections in place. We do not see any future movement in this whilst the current protections remain in place.

- Q14) Do you agree that the MPF is a more effective tool than the REC to help reduce some of the barriers to water efficiency in the business retail market? Please explain your answer and provide supporting evidence.

W2B: We do not believe that either the MPF or the REC help reduce barriers to water efficiency as the MPF fundamentally protects poor performing retailers and the REC stops retailers from making enough money to support water efficiency.

- Q15) Are there ways in which our review of the REC could be used to strengthen incentives for business customers to use water more efficiently? Please explain your answer and set out how your proposal would benefit customers.

W2B: If you remove the cap, it will generate additional revenue for retailers to support the market with efficiency and it with the increased cost of water and wastewater services, and with the remove of caps, this will incentivise customers to make more use of efficiencies.

- Q16) Do you agree that any revised price or non-price protections resulting from our review should apply over a medium time horizon of 3-5 years? Do you think there are any significant factors or arguments that would point to either a shorter or longer duration?

W2B: Three years is sufficient; however, the pandemic has shown the need for the opportunity to review regulations in the event of unforeseen circumstances that impact the whole market.

- Q17) Do you have any views on the extent to which Ofwat could or should amend its approach to the monitoring and enforcement of REC price and non-price protections? In putting forward any views on any preferred approach, please explain how you think customers' interests would be best protected.

W2B: In removing the protections you will empower the customer to act on their own interests and fundamentally vote with their feet.