

By email

16 May 2023

OFFICIAL

Request for Information – Condition A8 of Water Supply and Sewerage Licence Standard Conditions

Dear Licensee

Strengthening Ofwat's monitoring and oversight of Retailers' financial resilience and understanding of governance structures

Since the business retail market opened in April 2017, Ofwat has been closely monitoring the development of the market to inform and support its regulatory approach and to ensure Ofwat is best placed to protect the interests of current and future business customers.

In accordance with our general duty under Section 27 of the Water Industry Act 1991 (the 'Act') to keep matters under review, we are continually reviewing our approach to monitoring the development of the business retail market. One area that we are keen to strengthen our oversight of is in relation to the ongoing financial resilience of Retailers who are operating in the market. We are also keen to better understand the role their corporate structures and governance processes play in supporting and enabling them to carry out their licensed activities. We set out the rationale for strengthening our monitoring of Retailers' financial resilience and our understanding of governance processes later in this letter.

I am therefore writing to you to formally request information relating to your ongoing financial resilience and corporate governance arrangements. This letter is a formal Request for Information (RFI) under Standard Condition A8 of the Water Supply and Sewerage Licence (WSSL). This licence condition requires Retailers to provide Ofwat with such information as it reasonably requires for the purposes of carrying out its statutory functions under the Act and the Water Act 2014.

Please see attached the formal RFI spreadsheet and accompanying guidance document. To respond to this request for information, please complete and submit the RFI spreadsheet as well as an accompanying narrative document. The requested information should be returned by email to marketmonitoring@ofwat.gov.uk no later than **11am on 27 June 2023**.

We understand that you may consider some of the data and information you provide in response to our RFI to be commercially sensitive and confidential. Accordingly, and subject to our statutory duties, we do not intend to publish your response to the RFI. Whilst we cannot provide assurances specifically about how obtained information will be shared, your response would only be shared externally if there is a lawful reason to do so, for example in accordance with the Act. You should also be mindful of your obligations under competition law in sharing or discussing any aspect of your response with other Trading Parties.

Existing regulatory approach

Ofwat has implemented a [market monitoring framework](#) to support our regulatory approach since the market opened in 2017. In moving to rely primarily on ex-post regulation and our concurrent competition law powers, a post-entry monitoring framework that enables us to collect timely information has been essential in supporting our regulatory approach. The information collected from Retailers as part of this market monitoring framework has supported timely and effective regulatory interventions aimed at supporting the effective functioning of the market and delivering improved outcomes for current and future business customers. From the early development of the market, we have since developed and evolved our monitoring over time in order to better understand key market trends, obtain valuable information about how the market is delivering for customers and identify any key issues that are preventing the market from operating more effectively for customers.

In Ofwat's [decision](#), published in December 2022, on revised price protections for customers who have not engaged in the market, we signalled that we would be taking steps to increase our oversight and monitoring of Retailers' financial resilience. At present, we do not routinely collect detailed financial information from Retailers as part of our ongoing market monitoring framework.¹ Instead, we have historically relied on Retailers' annual Certificate of Adequacy submissions (a requirement of their licence) for assurance of Retailers' resilience for the forthcoming 12 months. While these submissions provide self-assurance from Retailers on their ability to meet the obligations of their licence, a review of the information required as part of the Certificate of Adequacy process has highlighted some shortcomings in the accuracy, and therefore reliability, of the assurances we currently receive, including that it does not provide direct visibility of their financial resilience on a regular basis.²

¹ In the absence of information regarding Retailers' financial position, to help inform our [decision](#) to provide additional regulatory protections in respect of excess bad debt levels as a result of the Covid-19 pandemic, we issued information requests to better understand the impact of Covid-19 on Retailers' ongoing financial resilience.

² As part of work to strengthen our ongoing monitoring, in addition to their Certificate of Adequacy submissions, this year we requested a supplementary verification report from Retailers about the key financial and operational risks they face and how they intended to manage these risks such that they would meet all of their obligations as a Licensee.

At present, we do not regularly collect information on the corporate and governance structures of Retailers beyond the information supplied in an application for a Water Supply and Sewage Licence. We therefore have limited understanding of how Retailers are structured and governed following their entry into the market.

Rationale for strengthening our monitoring and oversight of Retailer financial resilience and our understanding of governance arrangements

It is important that Retailers operating in the business market are appropriately financially prudent and resilient, are sufficiently resourced and can deliver a high-quality service to their customers. To strengthen our oversight of the financial resilience of the market, we are implementing a monitoring regime that will allow us to collect detailed financial information from all Retailers on a regular basis. Accessing relevant information on a timely and consistent basis will increase our visibility of Retailers' underlying financial resilience. With greater visibility, our monitoring will provide better forewarning of potential risks to Retailer financial resilience, strengthening our ability to take appropriate steps to protect the interests of customers, and to minimise the impact on Wholesalers and the market as a whole.

Furthermore, we are taking steps to increase our understanding of the ownership structures of Retailers, the way in which their Boards operate, and their governance and decision-making processes. Collecting information on these topics will improve our insight into the businesses that operate in the market and the way in which Retailers are funded and governed. This insight aims at increasing our understanding of the risks in the market and improves our ability to take proactive steps to protect the interests of current and future business customers. It is not our intention to use the information we have collected to make regulatory decision(s) on the appropriateness of certain governance or ownership structures in the market, recognising that variation is appropriate for different Retailers.

We consider that this change in our monitoring approach will facilitate our duties set out in Section 2 of the Act, namely, to further the consumer objective to protect the interests of current and future business customers. We consider that increasing our visibility of Retailer financial resilience is consistent with Ofwat's approach to monitoring financial resilience of appointed water companies, where measures have been introduced to reduce the risk that a company's poor financial health may pose to the investment and performance improvements needed to protect customers and the environment.³

In setting out this approach, we have also had regard to the [English and Welsh Strategic Priority Statements](#), specifically the relative Government's expectations on Ofwat to 'reduce

³ [March 2023 Decision - financial resilience proposals to modify the ring-fencing licence \(ofwat.gov.uk\)](#)

potential disruptions to customers' access to retail services in the event of a Retailer making an unplanned exit'. It is important to note that in moving to a strengthened monitoring framework, the intention is not to seek to design a zero-risk supplier failure regime, noting that the entry and/or exit of Retailers can be consistent with a well-functioning market. We are mindful that our monitoring of Retailers' financial resilience does not, and cannot, provide perfect foresight of the risk of Retailer failure, as we have observed the sudden and unforeseen exit of Retailers from this and other markets in the past. However, increasing our awareness of Retailers' structures and their ongoing resilience does strengthen our ability to take appropriate steps to protect the interests of current and future business customers.

Experience from the business retail market and other sectors has highlighted the importance of increased awareness of Retailers' resilience. The impact of the Covid-19 pandemic on business customers and Retailers, and our [decision to provide additional regulatory protections](#), highlighted the importance of improving our visibility of Retailers' financial position and resilience, noting that Retailers reported varying levels of elevated bad debt costs across the relevant period. Furthermore, we are mindful of the [lessons learnt from the recent series of energy supplier failures](#) that highlighted the important role of proactive monitoring, alongside robust entry requirements, in supporting financial resilience in the sector.

Businesses in scope of this information request

This information request relates to information pertaining to a Licensee's entire non-household water retail business activities across the whole of the UK. To promote the submission of accurate and consistent information across the sector, the scope of this information request concerns Retailers' entire non-household water retail business such that this information can be reconciled to filed and published statutory accounts. For further detail, please refer to the accompanying RFI guidance document.

Licensees whose retail authorisation is restricted to self-supply are excluded from the scope of this information request.⁴

To note, both Dwr Cymru and Hafren Dyfrdwy are included in the scope of Ofwat's financial resilience monitoring framework for Wholesalers (i.e. appointed water and/or sewerage companies), and therefore have been excluded from the scope of this information request and the non-household financial resilience monitoring regime.

⁴ Some licensees may be limited to providing water supplies or sewerage services to their own sites and those of persons associated with them (known as self-supply). Self-suppliers have been excluded from the scope of this RFI.

Information collected in this request

Recent experience from the business retail market and other sectors has highlighted the importance of regular and up to date information on which appropriate regulatory decisions can be taken that are in the interests of customers. However, we are also mindful of keeping any reporting burden proportionate; balancing the regulatory burden for Retailers with the resource commitment from Ofwat to collect and understand financial resilience data on a regular basis.

While we recognise that we are asking for new and detailed information, we have sought to ensure we are seeking only information that we consider necessary to enable us to fulfil our functions; in this context, this is related to our visibility of Retailers' ongoing financial resilience and understanding of their governance arrangements. We have, where possible, also considered what information is already included and accessible in Retailers' published and filed annual accounts, and what aspects of Retailers' business structures we have limited visibility of.

Further details and guidance regarding this information can be found in the accompanying RFI guidance document.

Future information requests

To ensure we have access to the relevant financial resilience indicators on a timely and consistent basis, we intend to issue a further Request for Information in November 2023, with information being collected biannually thereafter on an ongoing basis.

Having regard to the Principles of Best Regulatory Practice, we are mindful of the need to ensure that we are only seeking information that is necessary. However, our ongoing monitoring must also remain adaptable to any developments that may affect those operating in the market, including where we see value in more detailed and targeted monitoring should we have concerns regarding a Retailer's financial resilience, instead of a 'one size fits all' approach. Therefore, while the subsequent information request is likely to include similar components to this RFI, our monitoring must remain adaptable to market developments, including where these reflect relevant macroeconomic factors, such that we maintain a comprehensive and up to date view of Retailers' financial resilience.

With the intention to review our approach to monitoring the market later this year, where possible, we will be seeking to align our increased monitoring of Retailer financial resilience with our future approach to market monitoring to ensure our monitoring framework remains proportionate, consistent and targeted.

Queries from Retailers

We recognise that this information requests comprises new and detailed financial information not previously collected as part of our market monitoring framework. As such, we invite Retailers to submit queries where clarification is required on any aspect of this information request and supporting guidance document. We will publish a list of queries received together with our responses on our website. Any queries regarding this information request should be sent to marketmonitoring@ofwat.gov.uk

Yours sincerely

Dan Mason
Director, Business Retail Market