

Water Bill

Reform of the water industry: retail competition

November 2013

This is one of a series of briefing notes on the Water Bill. Under the Water Bill, non-household customers will be able to change their water retailer. This note explains in detail how competition will work for customer-facing services in water. Further detail on the Water Bill can be found in other briefing notes.

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Retail competition

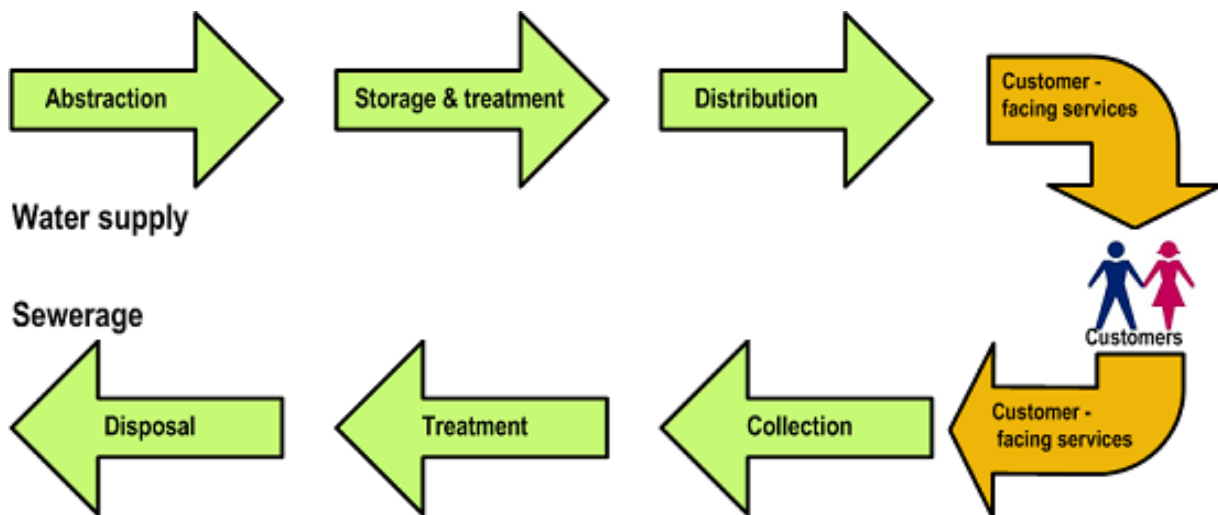
The UK Government’s vision is for a resilient and sustainable water industry, which is innovative and efficient, continues to attract long term investment and keeps customers’ bills affordable. The introduction of greater retail competition in England¹ through the Water Bill will help achieve this.

What are retail services?

These are all the “customer-facing” services that a water company typically provides. It includes billing customers for the provision of water supply and removal of their wastewater and sewage, handling their payments, reading meters and taking calls from customers about the network or other related issues.

Retail services are only a small part of what a water company does. For example, it does not include sourcing and developing sustainable water resources for public supply, water and sewerage treatment facilities or the management of a network to transport the water and wastewater. These activities are referred to as *upstream services*. Figure 1 below illustrates this.

Figure 1: The difference between retail and “upstream” services



* Green arrows = “upstream” services; Orange arrows = retail services

¹ References to England in this briefing note relate to customers served by incumbent water and sewerage companies located wholly or mainly in England (including Severn Trent); and references to Wales relate to customers served by incumbent water and sewerage companies located wholly or mainly in Wales.

What is retail competition?

Retail competition is when customers are free to switch from their local monopoly water company (the “incumbent water company”) to another water supplier. The Water Bill will allow some classes of customers to switch their water supplier (see below for more detail).

This does not mean that the water that comes out of their taps will be any different, or that it will come through different pipes. Their new water supplier (the “licensee”) will have to pay the incumbent water company an agreed price for the water and for their use of their network.

What retail competition already exists?

A small number of customers are already able to switch their water supplier, but everyone else has to stay with their local water company. That is because retail competition is currently limited to large, non-household customers (that is, businesses, public sector organisations and charities) who consume over 5 megalitres of water per year in England or 50 megalitres of water per year in Wales². No customers are eligible to switch their sewerage service provider under the current legislation.

While some retail competition already exists, it has not been particularly successful. The water consumption threshold has limited the size of the eligible market, and other factors set in legislation (in particular the costs principle) have made it unattractive to potential new water suppliers wishing to enter the market.

To date only four customers have switched their water supplier on certain sites since retail competition was initially allowed in 2005: C2C, Bernard Matthews, First Milk and Tesco.

The situation is different in Scotland, where all non-household customers have been able to switch their water and sewerage service supplier since 2008 when retail competition was introduced. While only 5% of their customers have switched their supplier, more than 45,000 customers (around 50%) have renegotiated the terms of their supplies and are enjoying a range of benefits.

What changes will the Water Bill make?

The Water Bill will enable all businesses, public sector organisations and charities, regardless of size, to switch their water supplier. It will also enable them to switch their

² Non-household customers located in England but served by water and sewerage companies located wholly or mainly in Wales are only eligible to switch water supplier if they meet the 50 megalitre/year threshold; conversely non-household customers located in Wales but served by Severn Trent are eligible to switch water supplier if they consume over 5 megalitres/year.

sewerage provider for the first time. These changes will be introduced in England (see Welsh Government position below).

The Water Bill will also enable cross-border arrangements with Scotland. This means a streamlined application process for potential water and sewerage service suppliers wishing to enter the market, and will ultimately mean that customers operating across England and Scotland will experience a seamless market.

The Bill will also make it more attractive for potential new suppliers to enter the market by changing the system of charges that incumbent water companies can levy on licensees for the use of the public water supply system. It will also ensure that all parties operate on a level playing field, governed by transparent rules and codes. This means that new businesses wanting to enter the market will not have to negotiate with the incumbent water company on a case-by-case basis.

Benefits of retail competition

Retail competition has benefits for customers, as well as providing opportunities to improve the efficiency of networks and to increase resilience.

Being able to switch water and sewerage service supplier will mean that businesses are free to negotiate for the best package that suits their needs; be it through more efficient customer service and better-tailored packages, water efficiency advice, or price. Research suggests over two thirds of small & medium-sized businesses support competition in the water industry³, and the public sector in Scotland is forecast to save over £36 million over four years from discounts to prices and new water efficiency measures.

Benefits are often more about the service than price. Large multi-site businesses, such as retail chains, hospitals and supermarkets, will be able to deal with one single supplier across England and Scotland for all their water and sewerage needs. This could significantly reduce their administrative costs. One business customer who receives over 4,000 paper bills a year for their different sites could save £80,000-£200,000 per year in administration if they moved to a single supplier for water and sewerage services⁴.

Large water users might look for a water supplier that provides them with better data on their water usage, smart metering, online support and advice on water efficiency to help them reduce waste. This offers obvious environmental benefits as water companies seek to attract new customers through new water efficiency services and advice. For example, in Scotland a water supplier helped a caravan park reduce their consumption by 20%

³ "Understanding the Needs of Small and Medium Enterprise Customers", Consumer Council for Water and Ofwat, 2012

⁴ "Water retail services competition in England and Wales: Still Hobson's choice", Policy Exchange, 2011
<http://www.policyexchange.org.uk/publications/category/item/water-retail-services-competition-in-england-and-wales-still-hobson-s-choice>

through installing rainwater harvesting. In another example, Business Stream estimates their water efficiency services in Scotland have saved customers over £13 million and saved 7.4 billion litres.

We expect that retail competition will have knock-on benefits for household customers as well, even though they will not be able to switch their water supplier. This is because they will benefit from improved customer service as their incumbent water company seeks to retain existing business customers and attract new ones in a more competitive market. This is one reason why the Government is not legislating to allow incumbent water companies to withdraw from providing retail services to non-household customers, as it will leave their household customers effectively “stranded” and suffering poorer customer service.

Retail competition also offers opportunities for economic growth. It will encourage incumbent water companies to be more efficient, and encourage new businesses to enter the market as water suppliers – potentially even offering multi-utility packages. We have already seen some organisations take advantage of the smaller, more restricted market we have now. Opening up this market to all business customers (not just large users), as well as creating cross-border arrangements with Scotland, will significantly enhance these commercial opportunities.

Why not let household customers switch their water suppliers?

The Government does not intend to extend retail competition to householders at this stage. There is no evidence to suggest it would provide enough direct benefits for householders, given the low margins involved in water pricing. The circumstances in which business customers are most likely to benefit from retail competition are not relevant to householders (unlike multi-site business customers, for example, who would benefit from one national bill).

Timetable

The new retail markets will be opened in England in 2017. The Water Bill will extend retail competition in England from around 27,000 non-household customers to a further 1 million customers. Before this can happen there needs to be considerable development and investment in an effective mechanism to allow customers to switch supplier, as the current switching mechanism was designed to allow for a small number of customer switches a year. This is being developed through the Open Water programme, which is run by the Government, Ofwat, industry and other stakeholders to develop the new markets.

Welsh Government position

The Welsh Government has taken the decision not to implement retail competition for incumbent water and sewerage companies operating wholly or mainly in Wales as they remain to be convinced that this will deliver any measurable benefits for Wales. The Welsh Government is developing an evidence base on mechanisms that will drive innovation and improvements in the water industry in order to secure the best outcome for Wales. The Welsh Government intends to set out proposed future policy options for Wales in their Water Strategy, which they intend to publish for consultation in January 2014.

The Welsh Government have taken a power in the Water Bill to implement retail competition in the future if evidence suggests that it will provide benefits for the customers in Wales.

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