

The Water and Sewerage Undertakers (Exit from Non-household Retail Market) Regulations 2016

Lead department	Department for Environment, Food and Rural Affairs
Summary of measure	The regulations gave water companies the option of exiting the retail market by transferring their non-household customers to one or more retailers, to enable all business customers in England to choose their water and sewerage retailer.
Submission type	Post-implementation review
Implementation date	3 October 2016
Department recommendation	Keep
RPC reference	RPC-DEFRA-5178(1)
Opinion type	Formal
Date of issue	25 July 2022

RPC opinion

Rating¹	RPC opinion
Fit for purpose	The PIR is now fit for purpose after being revised in response to the RPC's initial review notice (IRN). As originally submitted the PIR was not fit for purpose because the recommendation to keep the policy in place did not align with the evidence presented and the inter-relationship between this and preceding regulations needed clarifying.

RPC summary

Category	Quality²	RPC comments
Recommendation	Green	The issues raised in the RPC's initial review notice have now been addressed and therefore the analysis supporting the recommendation to keep the regulation in place is fit for purpose.
Monitoring and implementation	Satisfactory	The evidence informing this PIR has been gathered through workshops,

¹ The RPC opinion rating is based on whether the evidence in the PIR is sufficiently robust to support the departmental recommendation, as set out in the [better regulation framework](#). The RPC rating will be fit for purpose or not fit for purpose.

² The RPC quality ratings are used to indicate the quality and robustness of the evidence used to support different analytical areas. Please find the definitions of the RPC quality ratings [here](#).

Evaluation	Satisfactory	<p>interviews and written input from market participants (including retailers, wholesalers and company chief executives). The Department also made use of existing data and reports from Ofwat and the Consumer Council for Water, as well as consultation responses for the recent 2021 amending regulations. Overall, this appears to be a proportionate approach for the policy.</p> <p>The PIR lays out transparently where the policy has not achieved its objectives or where there have been unintended consequences.</p> <p>The PIR states that a cost-benefit analysis has not been conducted at this stage because the market is not mature enough but, following the RPC's initial review, now clarifies better the relationship between this policy and the Water Act 2014. To support this, it includes an initial assessment of the Water Act, but the RPC would advise that a full PIR for the Water Act is produced and submitted for scrutiny in due course.</p>
------------	---------------------	---

Summary of proposal

The 2016 regulations gave water companies the option of exiting the retail market by transferring their non-household customers to one or more retailers. They were intended to promote a well-functioning competitive market, to enable all business customers in England to choose their water and sewerage retailer.

It was intended that market forces would incentivise wholesalers and retailers to reduce their operating costs and prices, improve efficiency and increase service levels.

The 2016 regulations erroneously disapplied certain provisions to water and sewerage undertakers operating in retail exit areas wholly or mainly in England. The disapplied provisions meant that a developer had to apply to a retailer to request new connections for water and wastewater for their development. However, retailers were not choosing to undertake this work, as it is very technical. Retailers did not have the resources to undertake the work, and there is little profit margin in the service.

This was corrected in the Water and Sewerage Undertakers (Exit from Non-household Retail Market) (Consequential Provision) Regulations 2021, which reapplied the provisions.

Response to initial review

As originally submitted, the PIR was not fit for purpose. The emphasis in the discussion was on additional measures needed to support market mechanisms rather than the impact of the policy in delivering its objectives. This has since been improved.

Specifically, the RPC's initial review notice raised the following red-rateable issues that have since been addressed:

- **The recommendation to keep the policy in place does not align with the evidence presented and the discussion within the review. The PIR must explain more clearly why the current regulation is still needed and why, despite identifying unintended consequences which appear to require regulatory amendments, the overall recommendation is to retain the regulation.**

The recommendation to keep the policy in place appeared counterintuitive, particularly as all water companies have now exited the market. The revised PIR now explains that the regulation retains a framework that provides a level playing field and protections for customers in by ensuring a 'supplier of first resort' in the event of future exits. This justifies the decision to keep the regulation place more clearly.

- **While the regulation may still apply to New Appointments and Variations (NAVs) who want to exit the market, the process appears convoluted. The PIR needs to consider whether the regulation could at least be simplified to**

only apply to these providers, so that they do not need to enter and exit the retail market if they only want to act as a wholesaler. Otherwise, this does not appear to be a strong argument to keep the regulation as it is.

While acknowledging that this process is sub-optimal, the PIR now clarifies that NAVs are rare and that removing or amending the Retail Exit Regulations would be a disproportionate approach in resolving the issue. Instead, it recommends using additional non-legislative guidance to address the problem, which the RPC accepts is reasonable.

- **It is not clear why the PIR considers that the unintended consequences identified will be resolved using new legislation through amendments to the Water Industry Act. The PIR needs to explain why this route is preferred and what the inter-relationship is between the regulations.**

The PIR now explains more clearly the relationship between this and preceding regulations. As with the issue surrounding NAVs, the PIR now clarifies that an unintended consequence of the Retail Exit Regulations surrounding Temporary Building Supplies (otherwise known as 'building water', typically used during construction projects) can be resolved more efficiently in a new policy package. The RPC expects to review the impact assessments for this new package in due course.

Recommendation

The PIR appears to meet the minimum statutory requirement that it sets out in paragraph 3.1, and has opted for a 'medium' level of evidence.

As explained above, the issues raised in the RPC's initial review notice have now been addressed and therefore the analysis supporting the recommendation to keep the regulation in place is fit for purpose.

Monitoring and implementation

The evidence informing this PIR has been gathered through workshops, interviews and written input from market participants (including retailers, wholesalers and company chief executives). The Department also made use of existing data and reports from Ofwat and the Consumer Council for Water, as well as consultation responses for the recent 2021 amending regulations. Overall, this appears to be a proportionate approach for the policy, consistent with the expectations set out in the RPC's guidance on PIRs.

The RPC's initial review notice also made the following recommendations, which have since been addressed:

- **The PIR should also explain in clearer terms the issues surrounding data quality and how these might be addressed.**

The PIR acknowledges that the issues surrounding data quality persist, but a

data cleanse plan has been developed with industry “to improve data quality with the purpose of improving customer experience”.

- **Although the PIR states that the retail market in England is the first of its kind, the analysis would benefit from comparing the English market with that in Scotland to benchmark and show what has happened in the absence (and presence) of such a change.**

The PIR now clarifies that “*the transfer of non-household retail services from Scottish Water to a retailer did not require similar exit regulations... because there is only one state-owned water company in Scotland, and the retail exit process could therefore be managed differently by the Scottish Government*”.

Evaluation

The PIR explains that, as intended, the regulation enabled all incumbent water companies to exit the retail market within the first three years of the market’s existence. It also lays out transparently where the policy has not achieved its objectives or where there have been unintended consequences, including the lack of customer awareness of the market.

The PIR does not provide an overall cost-benefit analysis to assess the impact of the policy, and states that a more detailed analysis will be produced for the next version of this PIR, due in 2026. The PIR states that a cost-benefit analysis has not been conducted at this stage because the market is not mature enough but, following the RPC’s initial review, now clarifies better the relationship between this policy and the Water Act 2014. To support this, it includes an initial assessment of the Water Act, but the RPC would advise that a full PIR for the Water Act is produced and submitted for scrutiny in due course.

The RPC’s initial review notice also made the following recommendation, which has since been addressed:

- **The PIR explains that there has been very little incentive for customers to switch provider so far, since the cost savings they would make are not worth the time investment. The PIR should therefore provide some discussion on why this was thought to be a potential benefit to customers in the first place, and evidence on why the ideal circumstances have not materialised.**

The PIR now elaborates on this point, stating that “*the opening of the market has had different impacts on different types of customers*” and that “*savings have been unlocked for some larger customers, and multi-site customers, where there is greater potential for streamlining through having a single national retailer*”. It also explains that low customer awareness remains a factor, particularly for small and micro businesses. The department should continue to monitor and evaluate this in future PIRs to demonstrate the success of the policy (and its impacts on the market), since this was seen as a key benefit.

Other comments

The PIR sets out qualitative evidence and research but would benefit from assessing the evidence from a broader perspective. For example, market consolidation is considered only in the context of economies of scale, and does not consider other impacts, such as customer choice, or other rationales for market concentration, such as ability of retailers to function in tight margins. In addition, the inclusion of data would substantiate the qualitative evidence from stakeholders that the PIR draws on to explain the market problems. As with the benefit to customers mentioned previously, the PIR should also look at why the expected benefits in innovation have not materialised.

While the PIR is short, it is difficult to follow for the lay-reader due to the technical nature of the policy and unexplained acronyms.

It also contains vague or passive statements such as “*We heard that...*” or “*We have observed some...*” which detract from the authority of the analysis presented and should be avoided.

Regulatory Policy Committee

For further information, please contact regulatoryenquiries@rpc.gov.uk. Follow us on Twitter [@RPC_Gov_UK](https://twitter.com/RPC_Gov_UK), [LinkedIn](#) or consult our website www.gov.uk/rpc. To keep informed and hear our views on live regulatory issues, subscribe to our [blog](#).