

Severn Trent

Response to proposed amendments to licence conditions for Direct Procurement for Customers

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WONDERFUL ON TAP



Response to amendments to licence conditions for DPC

About the consultation

Ofwat has proposed a set of amendments to the licence conditions for the six water companies that PR19 confirmed will deliver schemes through direct procurement for customers (DPC). As Severn Trent was not one of these six companies, the licence condition changes would not apply initially – although they could come into play when we have confirmed DPC schemes to take forward.

In broad terms, the proposed licence changes would:

- establish the processes by which a water company could undertake procurement for DPC.
- permit a water company to pass onto its customers the charges payable to the DPC provider.
- create a specific interim determination mechanism for changes to price controls in relation to direct procurement for customers.

The type of consultation underway is the second non-statutory consultation on Ofwat's updated proposals on the required licence amendments. These proposals have taken account of the responses received on its initial consultation in February 2020. In turn, any comments and responses that Ofwat receives from this consultation will then go on to help inform the final form of the modifications, which it will hold a statutory consultation on later this year.

Broad response

Overall, we welcome Ofwat's updated proposals and the changes made in light of earlier responses from stakeholders. In particular, we support Ofwat's moves to simplify the process and manage the levels of admin needed. A good example of this is reducing the points at which an Appointee would need consent from Ofwat and replacing it with obligations to notify Ofwat in writing instead.

We also welcome the proposal for the interim determination process to include a trigger mechanism that specifically relates to DPC schemes. We've noted the plan for a reduced materiality threshold – at 2% of turnover, rather than 10% – which we think is a prudent move.

Beyond this, we would suggest that this threshold is monitored overtime to make sure it works as intended. We are aware that in future AMPs, water companies could propose joint schemes for water trading that will need to go down the DPC route. If one of these companies needs to take the lead for DPC, it seems logical to think that this should be the company that is in the best overall position to carry out this role. We therefore think it worth making sure the materiality threshold does not inadvertently change either the willingness of companies to take the lead or the choice of lead company. For example, we note that the financial value of the materiality threshold (rather than its proportionate value) will differ by company size, which in turn, could affect the relative willingness of large and small companies to take on the lead role. Should such a situation arise, then it may be worth considering if a materiality threshold based on the scheme size might provide a workable alternative solution.

Further considerations

DPC procurement process consents (Condition U 4.1)

We note that the consents to start a DPC procurement process could be issued in stages and that these consents could also be conditional. Given that this implies a range of possible outcomes, then some further clarity and insight could prove useful, particularly around (i) the sorts of conditions that may be imposed or (ii) the situations in which such conditions could be imposed. As the licence may not be the best place to include this extra information, our suggestion would be to consider whether an accompanying guide could provide for this instead.

DPC procurement process bidding and joint schemes (Condition U, paragraph 9)

In thinking about future schemes that companies put forward jointly, most notably water trading schemes, there may be a need to develop the DPC rules further, particularly around Condition U paragraph 9. The main question here is how the rules should apply for each of the companies that are behind the joint proposal. For example, should all those companies that are involved with a joint proposal be prevented from bidding in the subsequent DPC bidding process? Or should it just be the lead company? As it is realistic to think that future bids could easily involve three companies – even the three largest in the sector – there's a question whether ruling all these companies out from the DPC process would still result in the fullest amount of benefits being delivered for customers.

If the intention is not to see such a reduced field of bidders, we think that there are two possible ways forward. One would be to expand the rules to take account of joint proposals in a way that only rules out the lead company from bidding in the DPC process, thereby giving greater certainty as to who and who cannot bid in the DPC process. The other would be to make use of the existing arrangements that would prevent these companies from bidding without the prior written consent of Ofwat. This second approach has the advantage of allowing Ofwat to decide on case-by-case basis whether to provide such consent, but this approach may come at the cost and time of adding a further process into the mix.

Independent technical advisers (Condition U 11.6)

We think that it is helpful to have set an expectation that independent technical advisers should not do anything that would materially disrupt the relevant entity's business, unless it is essential for preparing their report. Where such material disruptions are necessary, we think that, in the first instance, individual companies should be able to work with the advisers to minimise the potential for such disruptions. In addition to this, it may be helpful for the licence to include a provision that sets a further expectation for the Independent Technical Adviser to give a reasonable period of notice to a company of material disruption, so that the company has the best possible chance to prepare and minimise the potential impacts on the business.