

Trading and Procurement Code

August 2018

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1 Introduction

The Affinity Water Limited Trading and Procurement Code (“Code”) sets out the policies, principles and requirements that will apply in respect of trades of water between Affinity Water and third parties including other water companies.

1.1 Why do we issue a Code?

Affinity Water recognises the benefits that water trading can provide for customers and the environment. Water trading can reduce the need for abstraction and can benefit customer bills by providing a more cost-effective solution than developing new sources within our supply area. Trades can be for potable, raw and part-treated water.

Ofwat also recognises the benefits of water trading and offers a water trading incentive to water companies it regulates to encourage water trading to take place. However, it is important that customers and the environment are protected. Our Code ensures that the trades that Affinity Water makes align with the interests of customers, water companies and the environment.

We invite any party that wishes to offer to us a reasonable volume of reliable, sustainable and cost-effective water resources to contact us. We are similarly interested in any opportunities that a party can identify for us to provide water to them. Our Code provides with the information they need to be able to identify water trading opportunities and to understand how we will work with them to realise these opportunities.

Our Code has been prepared in accordance with Ofwat’s Trading and Procurement Codes – Guidance on Requirements and Principles dated May 2018 and has been approved by Ofwat.

<https://www.ofwat.gov.uk/publication/trading-and-procurement-codes-guidance-on-requirements-and-principles/>

1.2 Using the Code

We will keep this Code up to date and publicly available via our website. The approved Code will also be available on the Ofwat website.

1.3 Understanding this document

The document is structured as follows:

- Section 1 introduces the Code;
- Section 2 describes Affinity Water and explains where information regarding our water resources position and our current water trades can be found;
- Section 3 sets out the key principles for water trades;
- Section 4 sets out the requirement that must be met in order for an export or import to qualify for an incentive payment to companies regulated by Ofwat;
- Section 5 contains a glossary of terms; and
- Section 6 provides links to useful supporting reference materials related to water trading.

Specific references are also provided by hyperlinks embedded in the document.

1.4 Contact details

Any queries in relation to this Trading & Procurement Code, Affinity Water's Water Resources Management Plan ("WRMP") or in relation to water trading generally should be directed to:

Mumin Islam
Affinity Water Ltd
Tamblin Way
Hatfield
Hertfordshire
AL10 9EZ

Email: mumin.islam@affinitywater.co.uk

- **East**, where we provide water to the Tendering peninsula, north east Essex including the towns of Harwich and Clacton on Sea, with a population of 158,000 people.

Our Central Region does not have a coastline and is surrounded by neighbouring water companies. There is an existing strategic network of pipes across the region which can be utilised to transfer substantial volumes of water. The Affinity Water Central Region shares borders with the following water companies:

- Thames Water
- Anglian Water
- Cambridge Water (South Staffs Water)
- Essex & Suffolk Water (Northumbrian Water)
- Sutton and East Surrey Water
- South East Water

Our Central Region has an inset appointment at Bishops Stortford.

Our Southeast Region shares a company boundary with South East Water and Southern Water, as well as a portion of the Kent coastline. Existing transfers link this region to neighbouring water companies which provide resilience to the region when extra water is required. Our Southeast Region has an inset appointment at Martello Lakes.

Affinity Water East Region is surrounded on its northern and western boundaries by Anglian Water, and a coastline along its eastern and southern sides. There are no strategic imports nor exports in this region. However, water is shared with Anglian Water which provides the operational resilience for this area (Ardleigh Reservoir).

2.2 Water resources

We manage our water resources on the basis of Water Resources Zones (WRZs), each of which is the largest possible area within which all resources, including external transfers, can be shared. Each WRZ represents one of the communities we serve and has been named after the major river serving the zone to reflect our vision to be the UK's leading community-focused water company.

- Affinity WRZ 1 (Central) is also known as Misbourne.
- Affinity WRZ 2 (Central) is also known as Colne.
- Affinity WRZ 3 (Central) is also known as Lee.
- Affinity WRZ 4 (Central) is also known as Pinn.
- Affinity WRZ 5 (Central) is also known as Stort.
- Affinity WRZ 6 (Central) is also known as Wey.
- Affinity WRZ 7 (Southeast) is also known as Dour.
- Affinity WRZ 8 (East) is also known as Brett.

We recommend that parties that are interested in trading with us review our WRMP. This is a statutory plan that sets out how we will manage and develop water resources so as to be able to meet our duty to supply customers with water. We prepare a new WRMP every five years.

Our current WRMP was published in 2014 and covers the period 2015 to 2040. It can be found on our website at <https://stakeholder.affinitywater.co.uk/water-resources.aspx>.

We are currently preparing our WRMP for 2019 which covers the period 2020 to 2080 and information about our proposed new WRMP can be found at <https://stakeholder.affinitywater.co.uk/water-resources.aspx>. We have advertised in OJEU for parties to put forward trades to be considered in our new WRMP.

We also publish key information to support the water resources market in accordance with Ofwat's Water Resources Market Information Guidance dated 11 October 2017. This information can be found on our website at <https://stakeholder.affinitywater.co.uk/water-resources-market-information.aspx>. We published this information alongside our draft WRMP and it will be updated within one month of publication of our final WRMP. We will continue to update this information periodically to ensure it remains up-to-date.

2.3 Water trading

We have a number of trades of water with our neighbouring water companies and with inset appointees. We report on our existing trades to Ofwat and this information is published on Ofwat's website at <https://www.ofwat.gov.uk/water-trading-bulk-supplies-register-2017-18/>.

Regional trading opportunities are considered by the Water Resources South East and the Water Resources East Groups. Affinity Water is uniquely a member of both and is at the forefront of future development of the WRSE Group, believing strongly in the benefits of collaborative working and cross-company and third-party solutions.

Our existing import and export points within our Central Region and our Southeast Region are illustrated in the maps below. We have no imports to or exports from our East Region but we do share the water from Ardleigh Reservoir with Anglian Water.

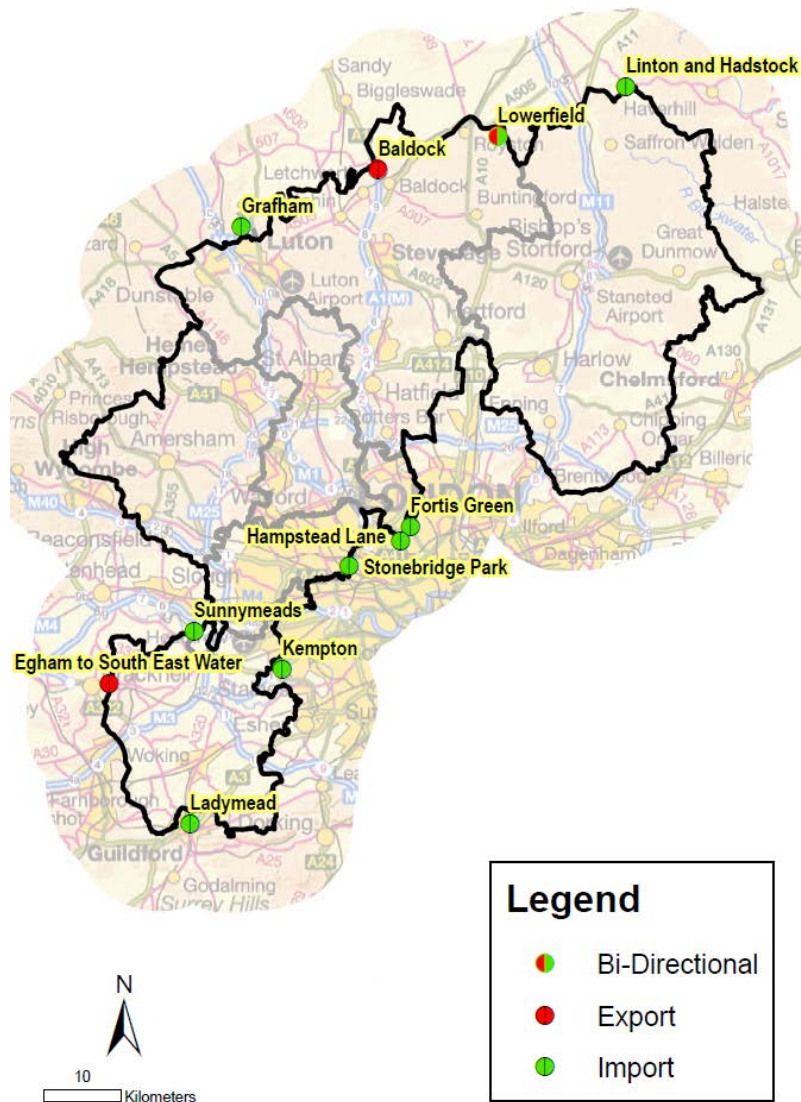


Figure 2. Map of Existing Import/Export Locations (Affinity Water Central Region).

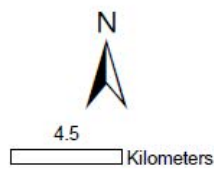
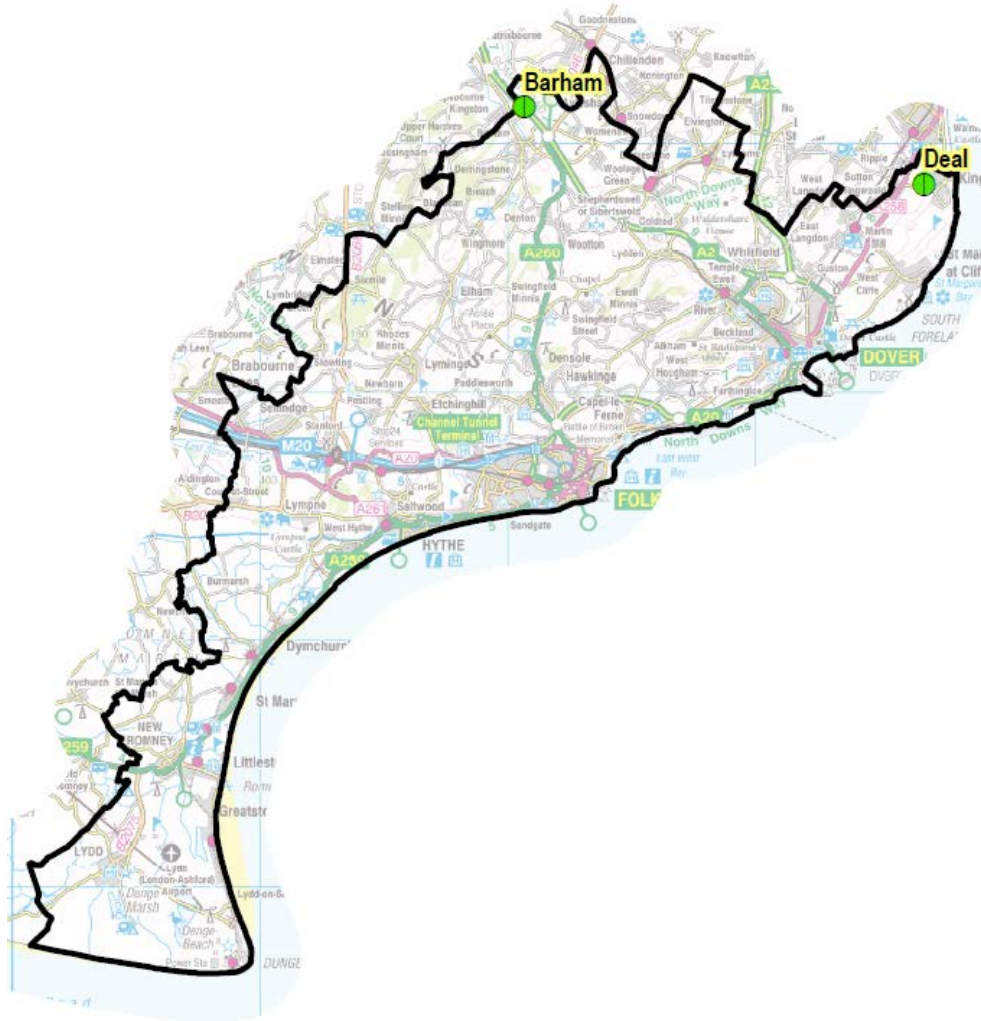


Figure 3. Map of Existing Import/Export Locations (Affinity Water Southeast Region).

3 Principles of the Code

Where trades are proposed between other water companies or third parties and Affinity Water, we are committed to trading in a transparent, sustainable and responsible manner, and to the benefit of our customers and the natural environment.

We are committed to the high-level principles identified by Ofwat and these principles will govern the way in which we negotiate and enter into water trading agreements.

3.1 Imports

3.1.1 Non-discriminatory procurement (Ofwat Principle 1)

We are committed to undertaking new trading discussions on a non-discriminatory basis. We will provide all parties with access to the same information by publishing water resources market information on our website (<https://stakeholder.affinitywater.co.uk/water-resources-market-information.aspx>). We will assess all potential trades against objective criteria set out in our Bid Assessment Framework which when published will be consistent with appendix 8 of Ofwat's PR19 final methodology <https://www.ofwat.gov.uk/wp-content/uploads/2017/12/Appendix-8-Company-bid-assessment-FM.pdf>

3.1.2 Economic purchasing (Ofwat Principle 2)

In contracting for the provision of water resources, Affinity Water will purchase from the most economic sources available, having regard to the quality, quantity and other relevant aspects. We will assess all potential supplies in accordance with our Bid Assessment Framework that will set out all the aspects to be considered and how individual supplies will be evaluated consistent with appendix 8 of Ofwat's PR19 final methodology <https://www.ofwat.gov.uk/wp-content/uploads/2017/12/Appendix-8-Company-bid-assessment-FM.pdf>

3.1.3 Use of competitive processes (Ofwat Principle 3)

Where appropriate, Affinity Water will seek to secure water supplies through an appropriate competitive process. We will invite potential suppliers to submit proposals when we are preparing our WRMP in order that these can be assessed against each other using our Bid Assessment Framework which will be consistent with appendix 8 of Ofwat's PR19 final methodology <https://www.ofwat.gov.uk/wp-content/uploads/2017/12/Appendix-8-Company-bid-assessment-FM.pdf>

3.1.4 Managing Imports

We manage our water supply over eight discrete WRZs. We will work with our trade partners to ensure water imports into Affinity Water are as efficient as possible. Existing assets will be used where possible.

3.2 Exports

3.2.1 Correct Assessment of costs (Ofwat Principle 9)

Affinity Water will ensure that its costs in providing an export are accurately estimated. Any estimate of costs will be based on all the costs of supplying the export including:

- maintenance of and operation of specific infrastructure in place to supply an export; and

- an appropriate share of the cost of abstraction, storage and pumping costs and other infrastructure used in providing the export.

Affinity Water will ensure that its charges under any agreement provide for full recovery of its estimated costs. We will include a price review mechanism within any agreement we enter into to ensure that agreements continue to provide for full cost recovery throughout the term of the agreement.

3.2.2 Managing exports

We will work with our trade partners to ensure our water exports are as efficient as possible, utilising existing assets and infrastructure to ensure costs are minimised where possible.

3.3 Exports and imports

3.3.1 Contract lengths (Ofwat Principle 4)

Affinity Water will ensure that the duration of its agreements for trading water are reasonable taking into account our need to have certainty regarding the resource available to us and the requirements of our trading partners who may have made significant investment to enable a trade to take place and may have their own statutory duties to meet.

We recognise the potential for water resources to change over the life of an agreement and for new trading opportunities to arise. Where appropriate we will include appropriate termination provisions within any agreement to respond to those changes.

Arrangements will be guided by the framework set in the Ofwat's Negotiating Bulk Supplies publication:

https://www.ofwat.gov.uk/wp-content/uploads/2013/08/pap_pos201308bulksupply.pdf

3.3.2 Transparency (Ofwat Principle 5)

Affinity Water is committed to effective provision of information to demonstrate compliance with the provisions of its Code. We will publish a short summary document for each new water trade we make to demonstrate how each trade meets the requirements of our Code. We will also arrange annual external assurance of Code compliance and will provide the results to our Audit Committee and to Ofwat.

We understand that the requirements of transparency must respect the commercial position of parties we are trading with and will not publish any information they provide to us on a confidential basis, except as required by law or a regulatory requirement.

Further information about the markets that Ofwat regulates can be found at <https://www.ofwat.gov.uk/regulated-companies/markets/> and to support the water resources market Ofwat also publishes market information which can be found at <https://www.ofwat.gov.uk/regulated-companies/markets/water-bidding-market/water-resources-market-information/>

3.3.3 Link to WRMP (Ofwat Principle 6)

Affinity Water adopts a single approach to agreeing water trading arrangements and selecting options under its WRMP.

The identification of potential deficits in the supply demand balance within a WRZ will be addressed by the analysis of all available options to provide new supplies and/or reduce demand including new water trading arrangements. Where we identify a surplus of water resources in a WRZ we will explore opportunities for providing water exports to support neighbouring companies.

3.3.4 Environment and Economic rationality (Ofwat Principle 7)

Affinity Water is committed to ensuring that any trades involve economically and environmentally rational flows.

We will assess all options available to us for securing our water resources on the same basis. This ensures that the trades we select are cost effective against all the other options we have available to us.

Where relevant, we will ensure that we only enter into a trade of water where an abstraction licence is in place and the Environment Agency has not indicated any change needs to be made to the relevant abstraction licence to deliver a sustainability reduction or other requirement under the Water Framework Directive.

We are working with Ofwat and the Environment Agency to develop and implement the Abstraction Incentive Mechanism (“AIM”) framework. The AIM will help to protect sources where there is a perceived marginal adverse environmental impact and alternative water sources or some other realistic means of reducing abstraction from the source are available and will not cause detrimental impacts.

3.3.5 No artificial ending of trades (Ofwat Principle 8)

Affinity Water will not artificially end and restart trades to take advantage of changes in incentive arrangements.

3.3.6 Appropriate allocation of incentives (Ofwat Principle 10)

Affinity Water will allocate any incentive payment that it receives to the relevant price control in accordance with the guidelines set out in Ofwat’s Final Methodology for the Price Review. We will allocate any export incentive in a manner consistent with the costs of making a trade and will allocate the import incentive based on the charges paid for the trade.

This will also depend on the types of trade i.e.

- Type 1: Source to source e.g. transfer of raw water from an exporter’s river abstraction source to the importer’s raw water reservoir source.
- Type 2: Source to raw water distribution/storage e.g. transfer from an exporter’s borehole into an importer’s raw water transport network
- Type 3: Treated to distribution network e.g. transfer from and exporter’s treatment works to an importer’s distribution network.

The allocation of the incentives for these types of trades will be consistent with the methodology set out on Ofwat’s website <https://www.ofwat.gov.uk/wp-content/uploads/2017/12/Appendix-5-Water-resources-FM.pdf> which includes details on the types of trades on pages 55-57.

3.3.7 Consistency with the company's bid assessment framework (Ofwat Principle 11)

This Code is consistent with and complements our Bid Assessment Framework, which will be published no later than 3 September 2018.

Further information can be found in Ofwat's publication <https://www.ofwat.gov.uk/wp-content/uploads/2017/12/Appendix-8-Company-bid-assessment-FM.pdf>

3.3.8 Evidence of assurance processes (Ofwat Principle 12)

We understand the need for robust assurance processes for the agreement of water trade arrangements to ensure decisions have a sound and objective basis and in particular take into account the long-term nature of water trading and supply-demand balances.

As stated in 3.3.2 we will publish a short summary document for each new water trade we make to demonstrate how each trade meets the requirements of our Code. The document will include a review of the processes followed during the trade negotiations. We will also arrange annual external assurance of Code compliance and will provide the results to our Audit Committee and to Ofwat.

Our WRMP is subject to an independent technical audit. The scope of this audit encompasses review of our decision making in selection of options and the robustness of our WRMP in balancing long-term supply and demand.

4 Qualifying Trades

This section explains the requirements that must be met for a trade to qualify for an incentive payment.

4.1 Agreement of trade in July 2013 or later (Requirement 1)

In order to qualify for trade incentives, the qualifying trade must have been agreed no earlier than July 2013. This means we must have signed a contract in relation to water trading arrangement in July 2013 or later.

4.2 The trade must be or have been operating between April 2015 and March 2025 (Requirement 2)

The import and export must have been operating between April 2015 and March 2025. This means the import or export must be operating in practice and revenues must have been generated under the water trading agreement during the price control period (1 April 2015 to 31 March 2020) or the price control period (1 April 2020 to 31 March 2025).

4.3 Trades to be between unrelated parties (Requirement 3)

A qualifying trade must be made between wholly unrelated parties that are not within the same group of companies.

5 Glossary

Term	Description
Abstraction	The process of removing water from the natural environment.
Abstraction Licence	The licence required to abstract water from the natural environment.
Affinity Water	Affinity Water Limited.
DEFRA	Department for Environment, Food and Rural Affairs.
Environment Agency (EA)	Regulator for the natural environment in England.
Megalitre (MI)	1 million litres of water.
Ofwat	The Water Services Regulation Authority (Ofwat) is a non-ministerial government department; they are the economic regulator for the water and sewerage sectors in England and Wales.
Potable	Water supplied for domestic consumption and/or food production purposes, as defined by WIA91.
Supply demand balance	A calculation undertaken through the water resources planning process to determine the balance (surplus or deficit) between the demand for water and available supplies.
Sustainability Reduction	Reduction in licensed abstraction required by the Environment Agency to ensure abstractions are not having a detrimental impact on the natural environment.
Water Resources Management Plan (WRMP)	A statutory plan which water companies use to plan ahead and manage their water resources.
Water Resources East (WRE)	The Water Resources East project brings together water companies, the Environment Agency, Ofwat, Consumer Council for Water, Natural England, Defra and other interested parties to consider the management of water resources in the Eastern region.
Water Resources South East (WRSE)	The Water Resources in the South East Group is an alliance of the six south east water companies, the Environment Agency, Ofwat, Consumer Council for Water, Natural England and Defra to develop long term plans for securing water supplies in the south east.
Water Trade	An agreement between a water undertaker and a third party including another water undertaker to transfer water between them.

Water Resource Zone (WRZ)	Water Resource Zone – the largest possible zone in which all resources, including external transfers, can be shared and, hence, the zone in which all customers will experience the same risk of supply failure from a resource shortfall.
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6 Useful Reference Materials

The following provides internet hyperlinks to documents relevant to this Code:

1. Water Acts

<http://www.legislation.gov.uk/ukpga/2014/21/contents/enacted>

2. Competition Act

<http://www.legislation.gov.uk/ukpga/1998/41/contents>

3. European Habitats Directive

http://ec.europa.eu/environment/nature/legislation/habitatsdirective/index_en.htm

4. Water Framework Directive

http://ec.europa.eu/environment/water/water-framework/index_en.html

5. Drinking Water Inspectorate

<http://www.dwi.gov.uk>

6. Environment Agency

<https://www.gov.uk/government/organisations/environment-agency>

7. Water for Life: Market Reform Proposals

<https://www.gov.uk/government/publications/water-for-life>

<https://www.gov.uk/government/publications/water-for-life-market-reform-proposals>

8. DEFRA 25 Year Environment Plan

<https://www.gov.uk/government/publications/25-year-environment-plan>

9. National Infrastructure Commission National Strategic Assessment

<https://www.nic.org.uk/assessment/national-infrastructure-assessment/>

10. Water Resources South East

<http://www.wrse.org.uk>

11. Water Resources East

<http://www.waterresourceeast.com>

