

This is a formal document that alerts our stakeholders on the way that we regulate the water sector in England and Wales.

## Licence fees for water companies and WSSL licensees

This information notice sets out how, when determining the level of licence fees, we will allocate relevant costs between companies holding appointments as water and/or sewerage undertakers (appointed water companies) and water supply and/or sewerage licensees (WSSL licensees). It replaces our October 2017 [Information notice 17/07 – Licence fees for water companies and WSSL licensees](#) (which has now been removed from our website). There have been no changes in relation to appointed water companies.

### Background

Both appointed water companies and WSSL licensees are required to pay licence fees in relation to the costs of the:

- Water Services Regulation Authority (**Ofwat**);
- Consumer Council for Water (**CCWater**); and
- Competition and Markets Authority (**CMA**).

These requirements are set out in Condition N (Fees) of appointed water companies' appointments and in Condition 9 (Licence fees) of Part A of the standard conditions of water supply and sewerage licences.

Some costs can only be recovered from one appointed water company or WSSL licensee. In other cases Ofwat needs to allocate costs between appointed water companies and WSSL licensees. We will, until further notice,

allocate costs in accordance with the method or general principles set out in this notice.

Part A sets out how costs will be allocated between appointed water companies. Part B sets out how costs will be allocated between WSSL licensees.

We are publishing this notice to reflect changes in how costs will be allocated between WSSL licensees.

The two changes we are making to the approach for determining WSSL licensees' fees reflect the conclusions in our [consultation response document](#) to our March 2018 consultation – 'Water Supply and Sewerage Licensing Regime: consultation on proposed changes to how licence fees are set'.

These changes are to:

- simplify the calculation of licence fees by calculating the flat fee element of

licence fees by licence for the costs of both Ofwat and CCWater; and

- include wholesale charges associated with transferred businesses in the previous year when calculating market shares.

We still think it is helpful to set out our approaches for apportioning licence fees for both appointed water companies and WSSL licensees in one document.

## **Part A: Method for determining a fair proportion of costs for appointed water companies**

Ofwat will determine the fair proportion of costs for each appointed water company in accordance with the following method:

### **1. General approach**

Subject to the following paragraphs, each appointed water company's fair proportion will be based on the percentage that the turnover of its Appointed Business\* (taken from the latest available regulatory accounts) represents of the turnover of the Appointed Businesses of all appointed water companies for the same period.

### **2. Price review costs**

Only appointed water companies for whom Ofwat will be setting price controls will contribute towards Ofwat's costs of preparing for or carrying out a Periodic Review\*. The fair proportion for each of those companies will be based on the percentage that the turnover of

its Appointed Business (taken from the latest available regulatory accounts) represents of the turnover of the Appointed Businesses of all of those companies for the same period.

### **3. Business retail market costs**

Costs in relation to the business retail market will be shared between WSSL licensees and appointed water companies. Only those appointed water companies whose areas are wholly or mainly in England will contribute towards the costs of Ofwat and CCWater in relation to the business retail market. 50% of Ofwat's relevant costs and 36% of CCWater's relevant costs will be allocated to those water companies (the rest being allocated to WSSL licensees). The fair proportion for each of those water companies will be based on the percentage that the turnover of its Appointed Business (taken from the latest available regulatory accounts) represents of the turnover of the Appointed Businesses of all of those companies for the same period.

### **4. Costs incurred by the CMA in relation to licence modification references for more than one company**

This paragraph applies where a reference mentioning more than one appointed water company has been made to the CMA under section 14 of the Water Industry 1991. The fair proportion of the CMA's costs for each of those companies will be based on the percentage that the turnover of its Appointed Business (taken from the latest available regulatory accounts) represents of the turnover of the

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\* These terms are defined in Condition A (Interpretation and Construction) of each water company's appointment.

Appointed Businesses of all of those companies for the same period.

## 5. Casework / Enforcement

This paragraph applies where Ofwat has to carry out work, such as special investigations or enforcement action, specific to certain appointed water companies. The costs of such work will normally be recovered from all appointed water companies in accordance with the general approach set out at paragraph 1 above. However, in accordance with established practice, subject to the relevant fee cap, Ofwat may decide to recover directly-attributable costs from the company or companies concerned if those costs are material and Ofwat considers that it would be unreasonable for other water companies to contribute towards some or all of those costs.

## Part B: General principles for determining a WSSL licensee's share of costs

Ofwat will determine a WSSL licensee's share of costs and any under-estimate or over-estimate in accordance with the following general principles:

### 1. Licence fees will be based on (i) a flat fee element per licence and (ii) a variable element based on market share that will reflect the bulk of costs

In summary the costs will be split the following way:

- 10% of the relevant costs of Ofwat and CCWater will be allocated as a fixed fee, divided equally by the number of licences for which a fee is payable<sup>†</sup>
- 90% of the relevant costs of Ofwat and CCWater will be allocated as a variable fee, based on market share.

The variable fee element will be calculated<sup>‡</sup> using:

- the wholesale charges to WSSL licensees in the preceding financial year (unless those charges will be used in the calculation of another WSSL licensee's market share); and
- the wholesale charges to an appointed water company's retail business or another WSSL licensee in the preceding financial year that relate to a retail business that has been transferred to the WSSL licensee.

### 2. Costs in relation to the business retail market will be shared between WSSL licensees and appointed water companies

50% of Ofwat's relevant costs and 64% of CCWater's relevant costs will be allocated to WSSL licensees (the rest being allocated to appointed water companies).

### 3. WSSL licensees supplying eligible Welsh customers will be charged on the same basis as WSSL licensees operating in England

### 4. Where a licence is granted during a financial year, no licence fee will be

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<sup>†</sup> Water supply licences and sewerage licences will therefore be counted separately because not every WSSL licensee holds both licences.

<sup>‡</sup> An illustrative example of the variable fee calculation can be found on p.9 of our [March 2018 consultation](#).

**charged to that licensee until the next financial year. The first licence fee then payable by such licensees will reflect a share of any under-estimate of the costs for the previous year but will not be reduced to reflect any over-estimate.**

**5. There will be no refund of licence fees paid where a licence is revoked mid-year**

**6. Self-supply WSSL licensees<sup>§</sup> will not be charged a licence fee**

**7. The CMA's costs in relation to any licence modification reference involving more than one WSSL licensee will be allocated on the basis of relative market share**

Any such costs are payable under Condition 9(4)(c)(ii) of Part A of the standard conditions of water supply licences and sewerage licences. The basis for allocating costs reflects

the principles set out in our March 2017 response document in relation to the variable element of fees. This general approach is also similar to that applied in relation to appointed water companies (where equivalent CMA costs are allocated on the basis of relative turnover).

Relative market share will be calculated by reference to the wholesale charges paid by the relevant WSSL licensees in the preceding financial year.

## **Next steps**

Appointed water companies normally pay licence fees at the beginning of each financial year.

We will issue annual invoices to WSSL licensees early in the financial year.

## **More information**

[WSSL licence fee consultation - Summary of responses and conclusions \(June 2018\)](#)

[Consolidated working copies of appointed water companies' appointments](#)

[Standard conditions of water supply and sewerage licences](#)

Ofwat (The Water Services Regulation Authority) is a non-ministerial government department. We regulate the water sector in England and Wales. Our vision is to be a

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<sup>§</sup> A self-supply WSSL licensee is one that can only supply water or provide sewerage services to its own premises or to the premises of associated persons.

trusted and respected regulator, working at the leading edge, challenging ourselves and others to build trust and confidence in water.

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