



Charges reform
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Dear Sir/Madam

Response to Ofwat's consultation on wholesale and retail charges for 2015-16

This response to the recent consultation on the above topic is on behalf of SSE Water Ltd (SSEW).

SSEW is a NAV appointee – its business model entails taking wholesale services from the local incumbent water companies at the boundaries of its portfolio of appointed areas and providing retail supplies to end users in those appointed areas, using local infrastructure that we provide.

The NAV form of competition has existed in the water industry for a few years, providing a choice to developers of sites as to who provides the water infrastructure at their development sites. The retail prices that a NAV appointee can charge its customers are regulated by means of a 'relative price control' whereby retail customers cannot be charged more than the equivalent retail charges of the incumbent water company. SSEW is therefore very interested in the distinction between retail and wholesale charges and the development of these charges, as they crucially affect the economics of the existing NAV form of competition.

We discuss a number of general points relating to wholesale and retail charges below and attach responses to some of the consultation questions as an appendix.

General Comments on Charging Issues

Information Requirements for retail charges

SSEW welcomes the comments in the consultation paper about the information requirements of NAV companies i.e. that NAV companies need certainty on the planned incumbent retail charges in the areas in which they operate, in order to be able to set their own retail charges that comply with relative price control requirements. We believe it would be useful if Ofwat continued its practice of setting out the expected timetable of events



relating to the annual change in charges in April 2015, by means of the customary Information Notice towards the end of calendar year 2014.

Wholesale Charges appropriate to NAV companies

There is some discussion in the consultation about the development of individual types of wholesale 'access charge' that implicitly form part of the bundled wholesale charges that will be published by incumbent companies for 2015/16 and beyond. As competition develops, it is recognised that different types of access charge will be required to enable and support that competition. SSEW believes it would be helpful for Ofwat to signal to incumbent companies the type of wholesale/access charge that will be appropriate for NAV companies from 2015/16 onwards as this form of competition, upstream from the prospective supply licensees, is already in existence.

Our expectation is that the charges from incumbents to NAV companies for bulk services on a wholesale basis should be set at a discount to the 'wholesale' element of large user tariffs. The reason for this is that the 'wholesale' charges under discussion are being developed for application to supply licensees from 2017 and will apply to water services delivered at the premises of the final retail customer whereas NAV companies provide their own local infrastructure and therefore receive bulk services from incumbents further upstream. It is relevant to note that in the power network industry, wholesale "use of system" charges are set by reference to the voltage level of the exit point where services are taken and that competitive local infrastructure networks are facilitated by this charge structure.

Avoiding wholesale/retail mis-match in charges

Our final point on the developing structure of charges in the water industry is that Ofwat should guard against any mis-match developing between wholesale and retail charges for particular elements of service. For NAV companies in particular, whose form of retail charges are prescribed by regulation, there is the risk of a mis-match developing between more 'cost-reflective' wholesale charges and the generally applicable form of retail charges. Surface water drainage, for example, is a charging category where this might occur.

We hope these comments are helpful and would be happy to discuss any point further if required.

Yours sincerely

Aileen Boyd
Regulation Manager



Appendix

Response to Consultation Questions

Q1 *Do you agree with the proposed approach to the development of charging arrangements in the 2015-20 period? If not, please explain and provide evidence for your view.*

We agree with the approach to charging arrangements set out in Appendix 2, whereby progressive revealing of information on incumbent supply chain costs for providing services allows more granular wholesale and access charges to be set, within an evolving structure of charges framework.

Q2 *Do you agree with the nominal 5% bill change as a threshold for undertaking impact assessments? If not, please set out an alternative threshold and provide evidence for this view. Should the same threshold apply to all customer types?*

Q3 *Do you agree with such a threshold being a short-term measure? If so, when should Ofwat remove such a requirement?*

Q4 *Do you agree with the draft schedule for presenting standardised charging schedule presented in appendix 7? If not, please provide alternative proposals.*

Q5 *Should charges associated with Open Water and market readiness be included as a separate increment to the volumetric charge in the wholesale charging schedule?*

We agree that this seems a reasonable approach.

Q6 *Beyond 2015, do you agree that wholesale charges should be published in advance of retail charges? If so, please provide views on how far in advance is appropriate.*

For water market participants downstream of incumbent water companies, it is clearly necessary for them to be informed of the upstream charges they will face before they can finalise their own charges for downstream market participants and/or end retail customers. From the perspective of new retailers entering the market from 2017, a period of three months or so would seem reasonable, although it would also be preferable to avoid the release of such information over the end of calendar year public holiday period. In the shorter term, before the opening of the non-domestic supply market, it would also be helpful for NAV companies to be made aware of the wholesale charges applicable to them a few weeks in advance of their application.

Q7 *Do you consider that Ofwat should require retail water bills to provide a breakdown of retail and wholesale charges?*

No.