

Sonia Brown
Markets and Economics Division
Ofwat
City Centre Tower
7 Hill Street
Birmingham B5 4UA

Direct dial: 01225 526348
email: andy.pymer@wessexwater.co.uk

4th July 2014

Dear Sonia,

Consultation on wholesale and retail charges for 2015-16 and charges scheme rules

Thank you for the opportunity to respond to this consultation.

The timescales between now and 2015-16 are short, and it is helpful both that the consultation has been published now and that it sets out an evolutionary approach to charging reform over the next five years.

For the 2015-16 charging year as much further clarity as early as possible would be very helpful, in particular:

- we would be very happy to review an early draft of the charges spreadsheet during August
- and for there to be an earlier discussion and agreement of retail default tariff structures in the PR14 process

In our view all companies should have in place a medium-term charges strategy which would outline at any one time:

- the likely trajectory of charges for the main customer groups in the following 3-5 years,
- how they intend to balance the need for cost reflectivity with bill stability, and
- the strategies employed to protect customers.

Where the company is the monopoly provider of services companies should be required to consult annually on this strategy with customers and their representatives via each company's customer panel and have regard to the views expressed.



Taking this approach will encourage ongoing customer engagement and foster greater company ownership of charges. In contrast, the proposal for separate Impact Assessments each time a fixed threshold of bill change for individual tariffs is breached, could foster a "tick-box" approach to compliance.

We answer the questions to the consultation in the attached appendix. We also provide an alternative wholesale charging schedule which allows us to fit our charges into a common format.

We look forward to working with you to deliver these charging reforms over the coming months. If we can assist in this area in any way please do not hesitate to contact me.

Yours sincerely

Best wishes,

Andy

Andy Pymer
Director of Customer and Retail Services

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.

Arrangements for 2015-16

As we stated in our response to Ofwat's consultation on wholesale and retail charges, the most critical area is to ensure charges for 2015-16 are accurate and there is enough time for companies to make changes to their processes and systems. This new consultation gives a useful start, however the timescale to provide charges for next year is tight. The most pressing issues for us are as follows:

- Early sight of the charges spreadsheet – a draft could be sent to companies for comment before its publication in August
- Early discussion and agreement of Default Tariffs for the non-household retail price control

The rest of AMP6

For the remainder of the 2015-20 period, we support the evolutionary approach Ofwat is proposing.

The need for robustness of data forming a solid foundation on which solid charging arrangements can be built is paramount.

A lot of work has been undertaken over the last few years to create robustness in costs for the four new price controls through the Accounting Separation process. We think that these established methodologies should now be held stationary in order for robust charges to be developed above them. This will give more chance that the charges arrangements for the future will be successful and gain customer legitimacy.

However, many of the key questions on cost reflectivity have yet to be answered such as the appropriate allocation of the capital value discount and returns across the value chain and the use of long run marginal costs. While these questions will need to be answered when considering up-stream access prices they must also be reflected in wholesale charges.

Companies will have been developing charging strategies that assume certain approaches on these items and will be developing alongside this strategies to mitigate incidence effects and will be consulting and communicating these to customers. There is a danger that credibility of the process is lost if at a later date a regulatory decision requires these changes to be reversed.

We think that the onus should be on companies to make the case for making changes to the Accounting Separation methodology if the existing rules are shown not to be appropriate.

We agree with the proposals for cost reflectivity. We do not think that additional requirements are needed and companies are best placed to manage the tensions between cost reflectivity and bill stability in a proportionate manner.

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 for all customer types?

The previous charging regime benefitted greatly from a stable and well informed process enabling customers to be charged correctly and fairly; it is critical that future charging arrangements continue this legacy.

In our view all companies should have in place a medium-term charges strategy which would outline at any one time:

- the likely trajectory of charges for the main customer groups in the following 3-5 years,
- how they intend to balance the need for cost reflectivity with bill stability, and
- the strategies employed to protect customers.

Where the company is the monopoly provider of services companies should be required to consult annually on this strategy with customers and their representatives via each company's customer panel and have regard to the views expressed.

Taking this approach will encourage ongoing customer engagement and foster greater company ownership of charges. In contrast the proposal for separate Impact Assessments each time a fixed threshold of bill change for individual tariffs is breached in our view could foster a "tick-box" approach to compliance.

A review of tariff changes over the past five years shows that a 5% bill change at the individual tariff level may require large numbers of impact assessments and may create an unnecessary burden if the company has demonstrated its overall approach is reasonable and proportionate.

In recent years where our K factor has been 0% to 0.3% the evidence shows that the range of change at the tariff level is significantly different from the average bill change. This is due to differences in water and sewerage bills, changing volumes between customer groups, periodic updates of costs etc.

We agree with the principle of bill stability and the need for flexibility in reducing incidence effects for customers. We understand the need to manage bill changes in an appropriate way. However we do not think that the requirement to provide an impact assessment for every tariff that changes by more than 5% is appropriate.

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

We disagree with the need for a threshold.

Q4 Do you agree with the draft schedule for presenting standardised charging schedule presented in appendix 8? If not, please provide alternative proposals.

We agree with having a standardised wholesale charging schedule. It will give better visibility to customers, companies and potential entrants to the competitive market.

We propose some alterations to the draft charging spreadsheet that allows us to complete it with our current charging structure. We have attached a spreadsheet as part of our response to the consultation.

We have a number of large user tariffs which provide discounts based on differential network characteristics. We expect to fill in a separate draft schedule for each of these tariffs, as otherwise the draft schedule becomes unclear.

We have also added unmeasured supply and waste schedules in order to aid development in this area. These are much simpler than the measured schedules.

We have made the following refinements to the draft charging schedule shared in the consultation.

Measured supply

- Altered the volumetric bands to enable entering of volumetric and other fixed charges
- Added the provision for reservation charges

Measured waste

- Altered the meter size bands to enable entering of standing charges
- Allowed greater flexibility for entering standing charges as companies charge in different ways for drainage
- Added additional other fixed charges for large user tariffs' drainage charges
- Altered the volumetric bands to enable entering of volumetric and other fixed charges

Trade effluent

- Added the provision for fixed trade effluent charges
- Added additional other fixed charges for large user tariffs drainage charges
- Added volumetric bands to enable entering of volumetric charges

Finally, Ofwat needs to be clear whether the schedule determines the automatic application of a tariff or whether the schedule contains tariffs that a customer is entitled to apply for.

The approach we have always taken to charging is that customers have the choice of our entire tariff range rather than having a tariff imposed on them. Our preference would be for that to continue.

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

We agree.

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

We agree that wholesale charges need to be published over a reasonable timescale prior to the start of the new charging year. However, as retailers in the competitive market are not tied to the regulatory year of April to March charging, we do not think there is a necessity to mandate separate dates for the publishing of wholesale and retail charges.

There is a balance between giving stakeholders sufficient warnings of changes to wholesale charges and allowing wholesalers sufficient information to set wholesale charges accurately for the next year. It is in everyone's interests to ensure that wholesale charges are as accurate and stable as possible.

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

We expect companies will be required to publish separate wholesale and retail charges. We do not think it should be mandatory for companies to display wholesale and retail charges on the face of the bill. It is reasonable for companies to be transparent in their communications with their customers, but it would be unhelpful to mandate this split due to the potential for loss of bill clarity.