



Strategy & Regulation

Owat
Centre City Tower
7 Hill Street
Birmingham B5 4UA

Name Sarah McMath
Phone 0203 5778765
E-Mail sarah.mcmath@thameswater.co.uk

7 August 2015

Dear Sir or Madam

PR14 reconciliation rulebook - wholesale revenue forecasting incentive mechanism

Thank you for your invitation within the PR14 reconciliation rulebook policy document for views on the issue of consistency between the wholesale revenue forecasting incentive mechanism (WRFIM) formula and companies' licences. We understand that the options seek to address an issue of incompatibility with the licence, whereby companies could be unfairly penalised under WRFIM.

In our letter to Tim Griffiths at Owat on 10 July 2015, we set out that we would support the WRFIM formula change or a change to licence condition B to resolve this issue. We identified that the licence change had the advantage of giving companies more flexibility for bill smoothing during AMP6 (through maintaining WRFIM as a symmetric mechanism).

We provide responses below to each of the three points which Owat is inviting views on:

1. The potential drafting for a licence modification to allow the licence to be consistent with the original WRFIM formula

From our review of the potential drafting for the licence modification,¹ we consider that this would resolve the issue of incompatibility between WRFIM and company licences by making the WRFIM symmetrical without the need for a change to the WRFIM formula.

2. Whether companies would support such a licence modification

While we have not presented the licence modification to the Thames Water Utilities Limited Board during this short consultation period, we would recommend to the Board that they accept the modification if it was proposed by Owat.

¹ Owat, PR14 reconciliation rulebook policy document, page 55.

Thames Water Utilities Limited
Clearwater Court, 2nd East
Vastern Road
READING
RG1 8DB
T 0203 577 4989
F 0118 3738918
I www.thameswater.co.uk

Registered in England and Wales
No. 2366661 Registered office
Clearwater Court, Vastern Road,
Reading, Berkshire, RG1 8DB

3. Whether Ofwat should:

- **use the revised WRFIM formula for all companies;**
- **allow companies to choose between a licence amendment (and the original WRFIM formula) or no change to the licence (and the use of the revised WRFIM formula); and**
- **only introduce a sector-wide licence modification if all companies agree to the proposed change**

Our preferred option is to give companies the choice between a licence amendment or the WRFIM formula change to resolve this issue. This would protect customers (as companies would be incentivised to return over-recovered revenue to customers with a two-year lag under either choice) and gives those companies who prefer the licence amendment option greater flexibility to smooth bill impacts during AMP6 (consistent with Ofwat's original stated aim of WRFIM).

We consider that the first and third options above are unnecessary, as customers would be protected under either approach and there is no material benefit in having a consistent approach (e.g. the WRFIM spreadsheets for both the original and revised WRFIM formulae have already been developed).

Other comments

For information, when reviewing Ofwat's published WRFIM spreadsheet with the revised formula, we identified three minor errors which we would like to bring to your attention:

- On the 'WRFIM – Water' tab, the formula in cell L28 is picking up the FD allowed revenue from 2014-15 (cell K15) rather than the FD allowed revenue from 2015-16 (cell L15).
- Cell K15 in the 'WRFIM – Water' and 'WRFIM – Waste' tabs do not pick up the input cells in the 'Data' tab, because the name definitions for AllRev.Water and AllRev.Waste refer to an array instead of a single cell.
- The inputs in cells L27 and L28 in the 'Data' tab are in 2014-15 prices, which is what we expected, although the rulebook (page 55) refers to these as being input in 2012-13 prices.

From our review of the spreadsheet for the wholesale totex sharing mechanism, we have identified areas where changes to the spreadsheet published with the rulebook for consultation appear to be inconsistent with the final determinations and the rulebook policy document. We will contact Ofwat separately on these issues.

Page 3

We hope these responses are helpful. If you would like to discuss them further, please do not hesitate to get in touch.

Yours faithfully

A handwritten signature in black ink, appearing to read 'Sarah McMath', written in a cursive style.

Sarah McMath
Head of Strategy

