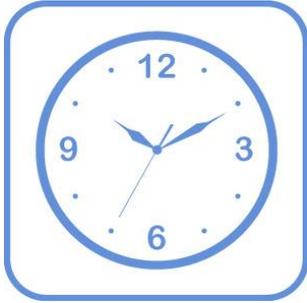




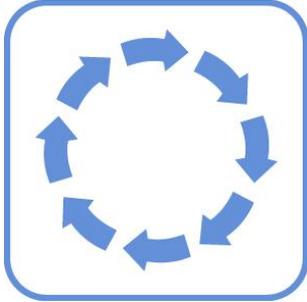
Charging workshop

12 September 2014

Agenda



Introduction and purpose	10 mins
High level overview of charging	20 mins
Charging publication	15 mins
Form of controls	20 mins
Social tariffs	10 mins
Coffee break	15 mins
Filling in the template	30 mins
Questions	30 mins



Introduction and purpose

For 2015-16 companies will need to publish separate wholesale and retail charges.

The governance arrangements are also changing.

Companies have requested this workshop to help improve their understanding around the changes.

This workshop will cover a few specific areas, and then will open to the floor for questions.



Background – Ofwat’s approach

Over the past few years we have increasingly sort to give companies greater accountability of their charges.

This has included approving charges based on companies’ assurances, taking an increasingly light touch approach, and only stepping in on a risk-based approach.

Likewise, through the price review process there have been some really positive examples of companies rising to the challenge, and producing customer-centric robust plans.

We would like to see this trend continue for how companies set their charges going forward.



Background – Water Act 2014

The Water Act 2014 complements Ofwat's overall direction of travel to date with regard to charging.

The Act seeks to remove the requirement for Ofwat to approve companies' charges, instead replacing the approvals process with a rule framework.

This would mean that companies can set their charges without Ofwat approving them. Ofwat would only get involved if the company did not comply with the rules.

While there is currently uncertainty whether a rule-based framework will be in place for 2015-16. If the relevant section is not brought into force in time, we will operate an approvals process in line with the spirit of a rules-based approach (i.e. clear company accountability).



Background – price review

The price review consists of four controls. Companies will need to set their charges in a way best calculated to comply with the controls.

Compliance will ultimately be assessed through the regulatory accounts. Failure to comply with the controls could result in a breach of licence and/or penalties under the revenue forecasting incentive mechanism.

Companies also have a range of other duties and obligations to take into account in setting charges. Such as, other licence conditions, the Water Industry Act, and competition law to name but three.

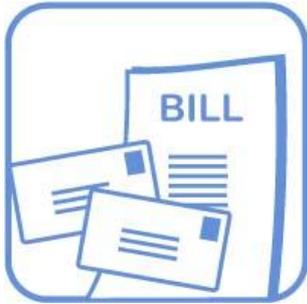


Risk-based approach

As there is a significant amount of change for 2015-16, we consider it to be appropriate to ask for some ex ante information regarding price control compliance and potential incidence effects.

On 29 August we published a spreadsheet for companies to complete by 3 October. The spreadsheet enables companies to provide us with information on the above stated areas. The information will be based on draft determinations, final November RPI figures will not be available.

Consequently, we may ask for a resubmission after the final determinations. However, we have not yet defined our final process – this will in part depend on whether the Act is commenced in time.



Charges publication

On 2 February companies will need to publish both their wholesale and retail charges.

In future years, we will require wholesale charges to be published earlier to enable new entrants to develop their own retail charging proposals ahead of the new charging year from April.

In developing charges for 2015-16, we expect companies to consult with CCWater, and to engage with their customers and their representative groups as appropriate. We expect companies to publish their charges in a customer-friendly, transparent manner.



Wholesale charges

As we confirmed in our consultation on wholesale and retail charges, for 2015-16 we will not require any form of wholesale standardisation to charging structures. However, to help provide a degree of transparency to retailers, we have consulted on a standard schedule (that was proposed and developed by companies) for non-household wholesale charges.

Companies can choose to set out their wholesale charges (both household and non-household) in any format they consider appropriate (as long as it provides suitable transparency), but the publication will need to include the standard schedule.

Companies that consider the schedule to not be consistent with their charging structures should inform Ofwat through their representations.



Wholesale

As we confirmed in our final methodology, we are using a total revenue control approach.

The controls will equal a total of revenue from charges plus income from new connections and infrastructure charges.

In the A8 charging appendix of the draft determinations, we set out the total allowed revenues in November 2013 prices (the required price base as per licence condition B).

As per the email sent to companies from portfolio leads on the 11th of September, there was a calculation error in the August table, this resulted in the figures being 3% too low. This will be corrected for the final determinations.



Household retail

As we confirmed in our final methodology, we are using a total revenue control approach with annual 'change factors'. That is, where customer numbers differ from forecast, an adjustment is made to the total allowed revenue.

In the company-specific appendices of the draft determinations we set out the total revenue figures, and the annual change factors.

A way of deriving the total allowed revenue is by multiplying the change factors by the forecast customer numbers.



Non-household retail

As we confirmed in our final methodology, we are using an average revenue per customer type control approach. The controls consist of two components; an allowed cost and an allowed net margin.

In the non-household technical appendix and the separate note for the four early companies, we set out the two components of the controls for each customer type.

As the controls include a net margin set as a percentage, the associated wholesale revenues are required in order to calculate the total allowed revenue.



Social tariffs

In information note IN 13/19, we stated that social tariff subsidies (including Watesure, and Welsh Water assist) should be allocated to the retail control.

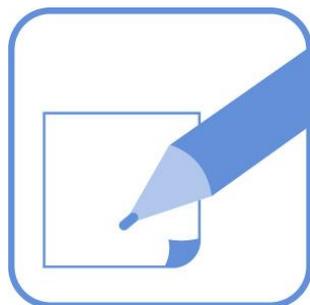
Therefore, there should not be different wholesale charges for a given customer type relating to whether or not they are on a social tariff. The subsidy needs to be administered through the retail control.

Surface water drainage concessions

In information note IN 13/19, we stated that surface water concessions should be allocated to the wholesale control.

Coffee break

Filling in the template



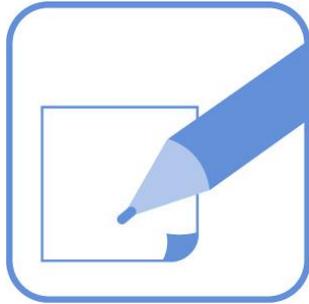
Bill effects

The purpose of this tab in the spreadsheet is to give us an early indication as to whether there are likely to be any significant incidence effects for 2015-16.

Companies need to identify at least 30 sample customers, and enter their charge and consumption data for 2014-15, and the proposed charges for 2015-16. The spreadsheet then calculates the change in bills.

Example:

Customer variable 1	Customer variable 2	Charge 1 (£) (2014-15)	Charge 2 (£) (2014-15)	Total bill (£) (2014-15)	Charge 1 (£) (2015-16)	Charge 2 (£) (2015-16)	Total bill (£) (2015-16)	Increase / decrease
1	1,000	30	0.5	530	25	0.45	475	9% decrease
Standing charge	1,000 cubic meters	Standing charge (£30)	50p per cubic meter		Standing charge (£25)	45p per cubic meter		



Revenue forecasts

The purpose of these tabs in the spreadsheet are to give us early visibility of any potential areas of significant under/over recovery.

As we confirmed in our consultation on wholesale and retail charges, actual compliance will be assessed through the regulatory accounts.



Wholesale

The spreadsheet enables companies to add different categories of wholesale charges. Companies are free to add more rows or columns if needed.

Multipliers are the aggregate basis for charging customers for each of the associated charges. For example, if the basis for the associated charge is to charge per customer, then the multiplier would be the total number of customers charged for that given wholesale charging category.

Wastewater includes trade effluent. Companies will need a wholesale charging category for each household and non-household retail customer type.

Other categories may be needed for where the company is supplying customers that are not on a default tariff.

Filling in the template

2014-15 prices	Allowed revenue (£k)
Water	
Wastewater	
Total	0.0
November 2013 RPI	252.1
November 2014 RPI	
RPI increase	-100.00%
K increase for 2015-16 water	0.00%
K increase for 2015-16 wastewater	0.00%

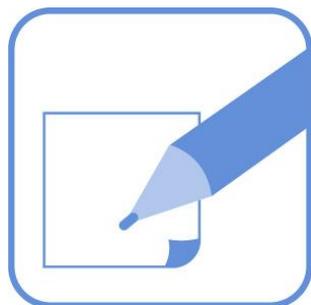
2015-16 prices	Allowed revenue (£k)	Revenue to be deducted (£k)	Wholesale charge revenue (£k)
Water	0.0		0.0
Wastewater	0.0		0.0
Total	0.0	0.0	0.0

Table A8.1 in the A8 Charging appendix

Forecast of November RPI

Forecast revenue and capital contributions from new connections

Filling in the cells indicated above, automatically calculates the (forecast) allowed wholesale charge revenue.



Household

The spreadsheet enables companies to add different bands of household charges. Companies are free to add more rows or columns if needed.

The spreadsheet calculates the total revenue recovered through the charges, and then deducts the associated wholesale revenue.

This leaves the household revenue forecast from the charges, which is compared to the forecast of allowed revenue.

Filling in the template

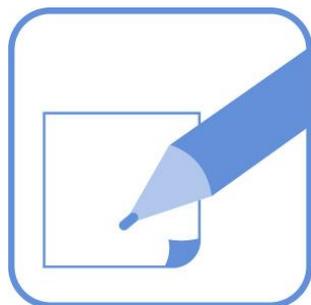
	Allowed retail revenue per customer (£)	Projected customer numbers	Allowed revenue (£k)
Unmeasured water-only customers			0.0
Unmeasured wastewater-only customers			0.0
Unmeasured water and wastewater customers			0.0
Measured water-only customers			0.0
Measured wastewater-only customers			0.0
Measured water and wastewater customers			0.0

These figures are in the annex to the company-specific appendices.

Note: the cost to serve figures given in the main document do not include the net margin. It is the revenue figures that are relevant.

Companies should populate their projected customer numbers for 2015-16. If a company has more up to date information than its business plan submission, it should use whichever forecast it considers will be more accurate.

Filling in the cells indicated above, automatically calculates the (forecast) allowed household revenue.



Non-household

The spreadsheet enables companies to populate data relating to their non-household customer types. Companies are free to add more columns if needed.

The spreadsheet calculates the total revenue recovered through the charges, and then deducts the associated wholesale revenue.

This leaves the household revenue forecast from the charges, which is compared to the forecast of allowed revenue

Filling in the template

	Associated wholesale revenue (£k)	Projected customer numbers	Allowed retail cost per customer (£)	Allowed net margin	Forecast revenue (£k)	Retail service revenue (£k)
Band 1 - [add description]					0.0	0.0

These figures need to link through from the wholesale tab

Companies should populate their projected customer numbers for 2015-16. If a company has more up to date information than its business plan submission, it should use whichever forecast it considers will be more accurate.

These figures are set out in annex of the A5 non-household technical appendix and the separate note for the four early companies

Filling in the cells indicated above, automatically calculates the (forecast) allowed non-household revenue.



Standard schedule

The standard schedule provides a means of presenting companies' wholesale charges for non-households in a standardised way.

As we stated in the charges technical appendix, companies should highlight through their representations any remaining aspects of the standard wholesale charges schedule that do not fit their charging structures, including clear proposals to address those issues.

Questions



Any questions?