November 2015

Trust in water

Consultation on the review of non-household retail price controls

www.ofwat.gov.uk

About this document

At present, only a limited number of non-household water customers across England and Wales can choose their retailer – but this will change significantly in April 2017. The Water Act 2014 will allow 1.2 million businesses and other non-household customers of providers wholly or mainly in England to choose their supplier of water and wastewater retail services. Retail services include:

- billing;
- meter reading; and
- other customer services.

This consultation is part of our work to ensure that the new non-household retail market operates in a way that is in the best interests of customers. It sets out the background to the introduction of non-household retail price controls from 1 April 2015 and seeks views on the best approach to reviewing these price controls ahead of market opening in April 2017.

We summarised our wider programme of work on protecting customers in the new retail market in an information notice on the opening of the retail market, which we published on 4 September 2015 (IN15/12: 'Opening a new retail market for non-household customers – protecting customers').

Contents

1. Summary and overview

Our December 2014 price control determinations (our 'final determinations') set the non-household retail price controls that will operate between 1 April 2015 and 31 March 2017 for the 18 major companies holding appointments as water or water and sewerage undertakers under the Water Industry Act 1991. The focus of this consultation is the review of these retail price controls so that we can set price controls from April 2017, when the English non-household retail market is opened to competition.

In 2014, the UK Government put in place legislation to facilitate the introduction of competition into the non-household water and wastewater retail market. This new market will be the largest retail water market in the world and should deliver substantial benefits to customers and the wider economy. Being able to switch water and wastewater retailer will mean that eligible customers are free to negotiate for the best package that suits their needs, including:

- better and more focused customer service arrangements;
- enhanced levels of advice on water management and efficiency; and
- prices and other terms and conditions of service.

It will provide opportunities for the best and most efficient retailers to grow and expand. Customers and the wider environment will also benefit from the development of new water management and efficiency services. And we expect that benefits will extend to customers that are not able to switch retailer, as innovative retailers identify better ways of doing things that can apply to all customers.

But experience in other sectors suggests that in the transition to full competition there may be a need for continuing regulatory protections – to shield customers from potential abuse associated with remaining pockets of substantial market power and to provide confidence that the new market arrangements will not unnecessarily disadvantage groups of customers.

This provides important context for this review of non-household retail price controls. We need to make sure that the price controls do not create undue barriers to entry or expansion, or restrict the ability of customers to secure deals with retailers that best meet their needs. At the same time, we need to ensure that basic protections are in place to promote trust and confidence in the delivery of vital water and wastewater services.

We considered these issues as part of the 2014 price review (PR14), and they informed the development of the default tariff price caps. However, as part of the process leading to our final determinations companies faced significant challenges in allocating non-household retail costs and margins to individual default tariff caps. Given this challenge, we set non-household retail price controls for a period of two years. This was to allow for a review ahead of market opening and for companies to be able to provide new evidence and, where appropriate, suggest changes to the way in which non-household retail costs and margins were allocated to the default tariff caps.

This remains our starting point for this review – that it is an opportunity for companies and other stakeholders (including customers and potential new entrants to the market) to comment on and provide evidence on companies' allocations of non-household retail costs and margins between the default tariff caps.

While we remain open to changing the scope for this price control review, we would only do so if we were satisfied that a different approach to that which is currently envisaged and set out in this consultation would better meet our statutory duties[1], including protecting the interests of customers (where appropriate through promoting competition).

Throughout this consultation, we raise a number of questions, which we summarise below. As well as responses to these questions we welcome views from stakeholders on any other issues that they consider important.

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[1] Our main statutory duties are to:

- further the consumer objective (to protect the interests of consumers, wherever appropriate by promoting competition);
- secure that the companies properly carry out their functions;
- secure that the companies can finance the proper carrying out of their
- functions; and
- further the resilience objective (to secure long-term resilience).

Subject to those duties, we also have duties to (among other things):

- promote economy and efficiency; and
- contribute to the achievement of sustainable development.

Key consultation questions

Q1 Should this review focus only on issues relating to the non-household retail price controls and the default tariff price caps?

Q2 In considering non-household retail issues, should this review allow for the reallocation of costs and margins between default tariff price caps, but with the constraint that aggregate levels of non-household retail costs and margins remain the same as in the existing controls, consistent with the expectations set out in our final determinations?

Other consultation questions

Q3 How can the transparency in the mapping of tariffs to the default tariff caps be improved?

Q4 Do you consider it appropriate to encourage companies to increase the consistency in default tariff cap structures and consider carefully whether the diversity in the present levels of default tariff caps is properly justified?

Q5 What information should companies be asked to provide and publish in support of any proposals (including for no change) they make in respect of their default tariff caps?

Q6 Do you consider it appropriate to allow companies the option not to update their cost and margin attributions and allocations, and so retain their existing default tariff price caps?

Q7 Is a three-year duration appropriate for the next non-household retail price control and if not what is the most appropriate duration and why?

Q8 Do you agree with the proposed timetable for this review, with a statement of method in April 2016, draft determinations in September 2016 and final determinations in December 2016?

We invite responses to this document by **11 December 2015**.

You can email your responses to NHHRetailPriceReview@ofwat.gsi.gov.uk or post them to:

Phil Griffiths
Ofwat
Centre City Tower
7 Hill Street
Birmingham B5 4UA.

If you wish to discuss any aspect of this document, please direct your enquiry to Phil Griffiths on 0121 644 7615 in the first instance.

We will publish responses to this consultation on our website at www.ofwat.gov.uk, unless you indicate that your response should remain unpublished. Unless there is a clear reason why your response should be confidential and not be published we may give less weight to such responses in reaching our decisions in matters related to this review.

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with access to information legislation – primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 and the Environmental Information Regulations 2004.

If you would like the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory 'Code of Practice' which deals, amongst other things, with obligations of confidence. In view of this, it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that we can maintain confidentiality in all circumstances.

An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on Ofwat.

2. Background

This chapter sets out background information to the setting of non-household retail price controls in 2014, including on:

- the form of the price controls;
- calibration of the default tariff price caps;
- compliance; and
- the duration of the price controls.

2.1 Form of the price controls

PR14 moved away from a single price control covering the whole supply chain and set separate price controls targeted on companies' wholesale and retail activities. This provided more effective incentives for the different parts of the value chain, and supported and facilitated the development of the competitive market for retail services to non-household customers. We set separate price controls on each of the following activities.

- Wholesale water.
- Wholesale wastewater.
- Household retail.
- Non-household retail.

All non-household customers of companies operating wholly or mainly in England will have the ability to choose their retailer from 1 April 2017. In 'Setting price controls for 2015-20 – final methodology and expectations for companies' business plans' (our 'price control methodology statement'), we committed to introducing default tariff controls to protect these customers[2]. The form of these price controls was designed to protect customers for the two years ahead of market opening and to provide backstop protection and a comparison point for customers once the market is open.

[2] We use the term "companies operating wholly or mainly in" to mean companies holding appointments as water and/or sewerage undertakers under the Water Industry Act 1991 whose area is wholly or mainly in England or, as the case may be, Wales.

When companies submitted their business plans in December 2013 there were a number of issues with their proposals for default tariffs. As a result, we removed default tariffs from our risk-based review and, following extended engagement with companies, adopted a form of control based on average revenue per customer for each tariff (the ‘default tariff caps’). Appendix A sets out the key publications issued during the development of the non-household retail price controls.

We based our final determinations on projections of total non-household revenue broken down into the following three components.

- The charges for wholesale services, which are collected by non-household retailers on behalf of the wholesaler.

- An allowance for non-household retail costs.

- A retail net margin (calculated as a percentage uplift on both the wholesale charges and retail costs) to provide for the efficient financing of capital employed in providing non-household services and reasonably remunerate risk.

The allowances for retail costs and net margins (when taken together these allowances are called the gross margin) were allocated to individual default tariff price caps. In effect, this form of non-household retail price control fixes the components of the gross margin (rather than total or average revenue) for each of the default tariffs. This means each company’s total non-household revenue will vary with changes to customer numbers (and so the control should automatically adjust for any loss of customers associated with the development of competitive pressures) and also with changes in wholesale charges as the net margins are fixed as a percentage uplift (to avoid changes in wholesale charges distorting competition).

Each company’s default tariff caps reflect its specific tariff structures, although a number of separate tariffs and/or charging bands may be linked to a specific default tariff cap. We did not impose a common set of national tariff caps consistent with each company’s ownership of its business plan and its structure of charges and to minimise possible incidence effects on prices for different customer groups. Given the complexity of company tariff structures, this has created a degree of complexity in implementing this form of price control.

The Welsh Government has explained that it remains to be convinced of the benefits of extending competition in the retail water market. So, it is not currently planning to extend competition for the non-household customers of companies operating wholly or mainly in Wales (Dŵr Cymru and Dee Valley) and that use less than 50 megalitres[3] (Ml) of water per year. In relation to these companies, the non-household price controls set at 2014 reflect the additional service and price protections that customers require in the absence of competition. The additional price protections take the form of a bespoke efficiency challenge on non-household retail cost allowances and lower retail margins (reflecting the absence of competitive pressures and lower risks).

2.2 Calibrating the default tariff price caps

As noted above, the non-household gross retail margins set for each company comprise:

- a non-household retail net margin; and
- an allowance for non-household retail costs.

Net retail margins were set an aggregate level for each company on the following basis.

- 2.5% for companies operating wholly or mainly in England and for the contestable customers of companies operating wholly or mainly in Wales.

- 1% for the non-contestable customers of companies operating wholly or mainly in Wales.

Companies allocated costs between wholesale, household retail and non-household retail activities.

In general, companies were required to absorb the impact of inflation on the future level of retail costs – so the aggregate level of retail costs was assumed to remain in line with 2013-14 levels for each year of the 2015-20 price control period. We considered a further efficiency challenge for companies operating wholly or mainly in Wales in order to offer additional customer protection to those customers who would

[3] A megalitre is one million litres.

not benefit from competition from April 2017. We applied this to Dee Valley Water as its business plan cost forecast was less challenging than the forecast implied by our analysis of the English companies' business plan proposals.

Each company then took the lead in allocating non-household costs and net margins to the individual tariffs. For each company, non-household retail costs were based on 2013-14 costs, with certain adjustments where specifically approved by us as part of the PR14 process.

The result of this process was an annual allowed gross margin for each non-household retail tariff, comprising an allowance for retail costs and a net margin. We call these allowances 'default tariff price caps'. Default tariffs are available to all relevant non-household customers in each company's area of appointment.

Appendix A includes further detail on the form of control.

2.3 Compliance

Since April 2015, companies have been responsible for setting charges for all non-household customers that comply with (that is, do not exceed) the default tariff price caps.

As competition develops (from April 2017) it will be important that companies have the flexibility to react to normal commercial incentives and seek to meet the needs and aspirations of their customers. For example, if companies wish to offer tariffs to customers that are below the default tariff price caps, then they may do so (as long as they comply with their competition law and other obligations) either by:

- setting tariffs below the level allowed by the default tariff price cap; and/or
- offering alternative types of tariffs to customers in addition to the default tariffs – in these circumstances customers would need to switch away from the default tariffs to the alternative tariff (rather than the company unilaterally transferring them).

As well complying with the default tariff caps companies must also continue to comply with their other charging obligations – including:

- those from competition law;
- the charging scheme rules established by Ofwat under section 143B of the Water Act 1991; and
- licence condition E, which prohibits undue discrimination or preference in setting charges.

2.4 Duration

At PR14 there remained significant differences between companies in the allocations of costs and net margins to apparently similar default tariff price caps. We therefore recognised that companies could benefit from having further time to:

- consider whether the default tariff caps were consistent with competition law obligations;
- gather evidence; and
- make representations to us ahead of the introduction of more competition into the non-household retail market in April 2017.

These considerations led to us proposing a two-year duration control, with a review in 2016. This timing would allow us time to implement any changes in the default tariff arrangements alongside wider market opening in April 2017.

While there was a clear rationale for companies operating wholly or mainly in England to be covered by such a review in 2016, there was a question about whether or not companies operating wholly or mainly in Wales should be included, given the difference in the policy positions of the Welsh and UK Governments in relation to introducing further retail competition. But both of the Welsh companies supported a review in 2016 and there are a small number of water customers in Wales (using more than 50 Ml a year) that will continue to be contestable under the new arrangements.

On balance, we decided that there would be benefits of having a sector-wide review in 2016, including companies operating wholly or mainly in Wales.

3. Key Issues

This chapter sets out our initial thinking on the key issues for the review of the non-household retail price controls in 2016, including the:

- scope of the review; and
- duration of the revised controls.

3.1 Scope of the price review

3.1.1 What we said in our PR14 final determinations

Our final determinations set out our expectations for the scope of the non-household price review to be carried out in 2016. We summarise these below.

- The key objective of the review would be to provide companies with the opportunity to refine their non-household retail cost and margin allocations between the default tariff caps to ensure that they are cost reflective and compliant with competition law.

- The scope of the review would be limited to non-household retail and we would not be considering changes to the household retail or wholesale price controls.

- We would not expect to consider new non-household retail cost claims from the companies and any reallocation of costs between the default tariff caps should not result in higher overall non-household retail cost allowances for each company.

- We would not expect changes in the allowed net margin in aggregate across non-household customer types – this should remain fixed at 2.5% as in our final determinations (for all companies operating wholly or mainly in England).

- The review would include all companies in England and Wales. However, if companies were to consider that their original allocations remain robust, they may have the option not to update their allocations.

- It would remain the companies' responsibility to ensure that their charges and practices are compliant with competition law.

3.1.2 New information

We have reviewed information that has become available after December 2014 as part of our work in assessing whether the above approach remains valid. In particular:

- in July 2015 regulatory accounts for 2014-15 were published, including information on non-household retail costs. Costs have risen across the sector, but some companies have managed to reduce costs. Given the limited amount of information available in these accounts, it is difficult to draw firm conclusions about the causes of these changes. The regulatory reporting requirements become more comprehensive in July 2016;
- the Competition and Market Authority's (CMA) provisional findings in its energy market investigation[4] have identified a number of issues, including that microbusinesses may not be properly benefitting from competition in the energy retail market. There are some similarities between energy retail and water retail markets and so this reinforces our view that a form of backstop protection for customers in the non-household water and wastewater retail market remains appropriate (until there is evidence that competition is sufficiently developed to protect the interests of customers);
- the CMA's findings in relation to Bristol Water's appeal[5] of its final determination did not make substantial changes to the non-household retail price controls; and
- consolidation in the non-household retail sector (South West Water and Bournemouth Water intend to combine their retail operations and create a separate non-household retail operation) demonstrates the potential for further innovation and cost efficiencies within non-household retail. The CMA has indicated in its provisional findings[6] that it will give unconditional clearance to this merger.

This information does not provide compelling evidence that we should change our broad approach to resetting the non-household retail price controls. While there is some limited evidence from the regulatory accounts that non-household retail costs have risen, there is also evidence of scope for corporate restructuring and cost efficiencies. It is also important that we retain the high level efficiency targets set out

[4] CMA, 7 July 2015, 'Energy market investigation – provisional findings'.
[5] CMA, 6 October 2015, 'Bristol Water price determination – summary of report'.
[6] CMA, 30 September 2015, 'The completed acquisition by the Pennon Group of Bournemouth Water – provisional findings'.

in our final determinations for the period 2015 to 2020 to provide overall incentives on companies to seek out and deliver new efficiencies.

In the case of non-household retail activities, there is likely to be no material loss of comparative information from corporate restructuring (including retail exit proposals discussed further below). As long as providers comply with the relevant legal requirements (for example, the consents for exit and licence requirements for arm’s length trading) and such arrangements do not cause a substantial loss of competition, then it is for companies to decide on and fund such changes, and benefit from the resulting efficiency gains. In due course, these will be shared with customers through the operation of the competitive market.

However, we have received a number of representations from potential market entrants in relation to the default tariff caps set in our final determinations. These include suggestions that:

- in the energy retail sector (where competition was introduced more than 15 years ago) the average cost serve to non-household customers is much higher than the allowances made in setting the default tariff caps;
- also in relation to the energy retail sector, as well as higher costs non-household retail businesses have higher earnings before interest and tax (broadly equivalent to the Ofwat allowance for net margin) and these higher margins are after the impact of price discounting;
- in the water sector non-household retail costs rose in 2014-15; and
- the non-household retail price controls set in December 2014 did not include a sufficient allocation of costs or margins.

We will consider these issues further together with the representations that we receive in response to this consultation.

3.1.3 Key questions for consultation

Our final determinations set out a framework to protect customers and encourage efficiency in the medium term. In the absence of compelling new information, there is a strong case for retaining the approach to this review that was envisaged in 2014 – with a focus on refining cost allocation issues between the default tariff caps and helping ensure that companies can comply with their competition law and other obligations. Wider issues, including around overall costs and margins, their allocation between price controls and whether price control protections continue to be required, could be considered at the next review of the non-household price controls when there is clear evidence about how competition is developing.

This approach should protect customers in the short term and build trust and confidence in the regulatory framework in the medium term by remaining open to change as competition develops to help protect customers. But it is important that consistency with our final determinations is not misinterpreted as unnecessary rigidity, and we will consider wider issues if new information emerges that suggests change is necessary to best protect customers. Bearing these considerations in mind, it would be helpful if stakeholders could comment on and, if appropriate, provide evidence in relation to our key consultation questions set out below.

Key consultation questions

Q1 Should this review focus only on issues relating to the non-household retail price controls and the default tariff price caps?

Q2 In considering non-household retail issues should this review allow for the reallocation of costs and margins between default tariff price caps, but with the constraint that aggregate levels of non-household retail costs and margins remain the same as in the existing controls, consistent with the expectations set out in our final determinations?

As we have explained above, we would require persuasive new information to widen the scope of this review or reconsider the basic assumptions on costs and efficiency that supported our final determinations. For the avoidance of doubt, these basic assumptions include the following.

- An overall non household retail net margin of 2.5% for companies operating wholly or mainly in England, and the contestable segments of the Welsh market. Our draft and final determinations published in 2014 considered a range of information on these issues, including evidence of the higher margins available in the non-household retail market in Scotland. We explained that there were a number of factors that explained these differences, including the different payment terms and working capital requirements applying in the Scottish market. This remains our starting point for this review, but we will consider any further information and evidence that emerges on these matters, including in response to this consultation

- An aggregate level non-household retail costs across all customer types as set out for each company in our final determinations. To protect incentives for efficiency, these allowances should not change from our final determinations (either to allow for increased or new costs or reductions in costs as a result of corporate restructuring or other efficiency savings arising since 2014).

- The further efficiency challenges set for Welsh companies should remain in place to continue to protect customers in the non-contestable section of the market.

A related set of issues to this review are the price protections that will apply to the customers of a company that holds an appointment as water or water and sewerage undertaker (that is, the companies that currently have default tariff caps), which seeks to exit its non-household retail obligations. In particular:

- the Water Act 2014 allows the Department for Environment, Food and Rural Affairs (Defra) to make regulations to provide for retail exit. This would involve an appointed company applying for permission to transfer all its non-household customers to a retailer holding a Water Supply and Sewerage Licence (WSSL), which could be an associated WSSL retailer or an unrelated WSSL retailer. Defra consulted on its proposed policy in December 2014[7], and has recently consulted on the draft exit regulations[8]. The Secretary of State will make decisions on retail exit applications;
- under the proposed exit regulations, Ofwat would be required to issue a retail exit code, which, among other things, may include provisions about the terms and conditions to be offered to customers affected by retail exit; and
- we will address the price protections that will apply to customers in the circumstances of retail exit in our consultation on deemed contracts, which will set out policy proposals for the retail exit code (the statutory code that will govern any such exits). Once we have considered responses to that consultation, we plan to develop the draft retail exit code, and consult on the draft code in February 2016.

3.1.4 The rebalancing of default tariff price caps

As noted in chapter 2, there is a degree of complexity associated with the default tariff caps. To some extent, this reflects the complexity in companies' charging arrangements. For instance, for a large customer its retail water and sewerage bill may have three components – water, sewerage and surface water drainage. In these circumstances, three separate default tariff price caps may apply with the overall gross retail margin associated with a particular customer deriving from the summation of these three default tariffs (including the percentage net margin mark-ups on the underlying wholesale charges).

[7] Defra, December 2014, 'Retail exits consultation document'.
[8] Defra, July 2015, 'Consultation on draft regulations'.

Also, for some companies it is not always straightforward to understand how their published charges map to their default tariff caps – particularly in relation to wastewater services.

Appendix B sets out a cross-sector comparison of the customer types, margins and cost allocations relating to charges for non-household metered water consumption. This shows significant diversity between companies in respect of the levels of default tariff price caps for apparently similar types of customer. Taken together, the above factors raise a number of challenges and issues.

- How to improve transparency so it is clear for all companies how published charges map to the default tariff caps.

- Whether the diversity in default tariff caps and the underlying tariff structures may create unnecessary complexity for potential new market entrants.

- It is not clear that all the differences in the levels of default tariff price caps for similar groups of customers reflect differences in underlying costs and instead may reflect differences between companies in the approach to the allocations of allowed costs and margins to customers with similar levels of consumption.

These factors suggest that there would be benefit in encouraging companies to make the following proposals as part of this review.

- Suggestions for improving transparency in the mapping of tariffs to the default tariff caps.

- Changes that would improve comparability between companies in terms of default tariff caps and tariff structures. In practice, this could mean allowing companies with complex default tariff cap structures to introduce reasonable simplifications, and those with the simplest structures to make modest increases in the number and cost reflectivity of their default tariff caps.

- Where supported by evidence that suggests the default tariff caps could better reflect underlying costs, then changes that would address the apparent diversity in the levels of default tariff price caps. In practice, this could mean allowing companies with a particularly high default tariff cap (relative to other companies) to rebalance by reducing this tariff cap but increasing its other tariff caps, and allowing companies with a particularly low default tariff price cap (relative to other companies) to rebalance by increasing this tariff cap but reduce its other tariff caps.

It would be the responsibility of companies to:

- manage potential incidence effects arising from any changes to default tariff caps;
- provide and publish strong evidence that they were engaging with their customers on a continual basis, and from this engagement and their day-to-day interactions with customers had gained support for any proposed changes to their default tariff caps or their decision not to update their allocations and retain the existing default tariff caps;
- provide and publish strong evidence that in overall terms any changes would be revenue neutral and consistent with the principle that the focus of this review is on reallocating costs and margins between tariffs rather than the overall level of the gross margin for non-household retail; and
- provide and publish a Board assurance statement on compliance with all their legal obligations (including the charging scheme rules established by Ofwat[9] under Section 143B of the Water Act 1991 and licence condition E, which prohibits undue discrimination or preference in setting charges) and competition law, assurance on incidence impacts and handling strategies, revenue neutrality, and the process the company has followed in engaging with its customers on its proposals for default tariff price caps.

As well as the baseline requirements outlined above, there is a question about what further information it might be appropriate for each company to provide and publish in relation to its default tariff caps. This should be considered in the context of our requirements (including our statutory duty to protect customers where appropriate through promoting competition) but also any legitimate concerns that potential market entrants and other stakeholders might have about proposals for changes to the default tariff caps. Further requirements to provide and publish information might include:

- information that shows that the allocation and attribution of costs and margins to the default tariff caps are reasonable and robust (with costs and margins attributed by appropriate drivers and activities, and the proportion of costs subject to broader allocation rules kept to the minimum that is reasonably practicable); and

[9] Ofwat, September 2015, 'Consultation on charges scheme rules for 2016-17 and future developments'.

- reasonable evidence (such as a report from expert consultants) that any proposals they make for default tariff caps (including proposals for no change) are consistent with competition law.

We would welcome views on what further information (if any) companies should be required to provide and publish as part of this review.

In relation to standardising default tariff caps and incidence effects there are clear inter-relationships with the development of both retail and wholesale charges. In our charges scheme rules consultation[10], we said that we will give careful consideration of whether and to what extent we should standardise or move to more comparable wholesale charging structures. We expect to consult on a set of proposals related to standardising wholesale charges in early 2016.

During PR14, customer challenge groups (CCGs) performed an important role in assuring both the quality of companies' customer engagement and the degree to which the results of this engagement were reflected in companies' plans. We expect companies to consider how they can best provide assurance that their default tariff caps proposals have been developed by customer engagement, including using their CCGs. We also expect companies to consider how best to use CCGs to provide assurance to us about the quality of their handling strategies in relation to any incidence effects.

The above considerations suggest the following questions for consultation.

Consultation questions

Q3 How can the transparency in the mapping of tariffs to the default tariff caps be improved?

Q4 Do you consider it appropriate to encourage companies to increase the consistency in default tariff cap structures and consider carefully whether the diversity in the present levels of default tariff caps is properly justified?

Q5 What information should companies be asked to provide and publish in support of any proposals (including for no change) they make in respect of their default tariff caps?

Q6 Do you consider it appropriate to allow companies the option not to update their cost and margin attributions and allocations, and so retain their existing default tariff price caps?

[10] Ibid

3.2 Duration of the controls and future developments

We are also seeking views on the most appropriate duration for the control to be set from April 2017. Our preferred approach is to set a three-year control to align with the existing controls for wholesale and household retail (which will end on 31 March 2020). This would allow us to both see how competition was developing in the non-household retail market and deal with any further cost allocation issues that might emerge between retail and wholesale and/or non-household and household retail.

Once we have substantive evidence on the development of competition we could also consider more substantial changes to the price control arrangements for non-household retail, including:

- deregulating those sections of the market where there is evidence that competition is effectively constraining prices; and
- simplifying the remaining backstop price arrangements for areas of the market where competition is continuing to develop, perhaps with a small number of national tariffs based on broad bands of wholesale charges and set as an overall percentage mark-up on wholesale charges.

This would be consistent with the broad thrust for our work on the Water2020 programme, with greater reliance on market forces to help protect the interests of customers.

We have also considered the following alternatives to the three-year price control duration.

- Set a shorter control of two years so that we can respond more quickly to initial evidence on the operation of the new competitive market. This would have the advantage of spreading the workload requirements for Ofwat, companies, and stakeholders. But, in practice, we would only have very limited information on the development of competition (given the need to allow time for a review process) and it would be more difficult to deal with cost allocation issues.

- Set a longer price control from 2017 (water company licences presently envisage retail price controls up to five years in duration). This would offer advantages in terms of spreading workload but this would not appear to allow for a timely response to emerging evidence on the development of competition and/or cost allocation issues.

Consultation question

Q7 Is a three-year duration appropriate for the next non-household price control and if not what is the most appropriate duration and why?

3.3 Timetable

In carrying out this review we are proposing to work to an indicative timetable broadly consistent with that published in the 2014 price control determinations, except for bringing forward the main submission of information by companies to allow for more time to consider issues and the evidence provided by stakeholders.

Table 1: Draft timetable for the 2016 non-household retail price control review

Date	Milestone
11 December 2015	Closing date for this consultation
8 April 2016	Ofwat publishes statement on method and data table requirements for the review
15 June 2015	Companies submit any changes to their cost and margin allocations **together with the data tables and supporting evidence**. These should be consistent with any relevant material information that will be available in preparing their audited 2015-16 regulatory accounts and regulatory reports
16 September 2016	Ofwat publishes draft determinations
28 October 2016	Companies and stakeholders respond to the draft determinations
16 December 2016	Ofwat publishes final determinations
1 April 2017	New non-household retail price controls and charges come into effect and the retail market opens

Consultation question

Q8 Do you agree with the proposed timetable for this review, with a statement of method in April 2016, draft determinations in September 2016 and final determinations in December 2016?

Appendix A: Further information

A.1 Form of price control

In our PR14 final determinations, we adopted a control in the general form of an allowed average cost per customer (rc), and a net margin (m) in line with our draft determinations and final methodology statement. This means for each customer type, for a given forecast of the customer numbers of that type on the default tariff in a given year, the forecast total allowed revenue from default tariffs offered to those customers will then be defined in the following formula.

$$R = [(rc \times cn) + w)] / (1-m)$$

Where:

R = the estimated total allowed revenue for a given customer type

rc = the allowed average retail cost component for a given customer type

cn = the forecast customer numbers for a given customer type

w = the forecast wholesale revenue for a given customer type

m = the allowed net margin for a given customer type

The customer numbers and wholesale revenues in each year will vary, while the allowed average retail cost component and margin will not. Accordingly, the forecast and actual allowed non-household retail revenues will vary each year.

We set out the detail of the final controls for each company in the company-specific appendices published as part of our final determinations.

A.2 Definition of retail

Our final determinations defined retail activities as including the following activities.

Customer services, including:

- billing;
- payment handling;
- remittance and cash handling;
- charitable trust donations;
- vulnerable customer schemes; and
- network and non-network customer enquiries and complaints.

Debt management and doubtful debts.

Meter reading.

Other operating costs, including:

- decision and administration of disconnections and reconnections;
- demand-side water efficiency initiatives;
- customer-side leaks;
- attributable other direct costs;
- attributable general and support expenditure; and
- attributable other business activities.

Developer services:

- providing developer information, and
- administration for new connections.

Attributable Business Rates (referred to as Local Authority rates in Regulatory Accounting Guideline – RAG – 4.04).

A.3 Development of the non-household retail price controls

The table below sets out a chronology and links to key documents published during the development of the non-household retail price controls set in our final determinations.

Document name	Publication date	Description/policy contents
'IN 14/01: Adapted approach for default tariffs' (our 'note on our adapted approach')	January 2014	Sets out our next steps for setting default tariffs following their removal from the risk-based review.
'Setting price controls for 2015-20 – risk and reward guidance' (our 'risk and reward guidance')	January 2014	Guidance on non-household net margin.
'2014 price review cost allocation for retail and wholesale price controls' (our 'guidance on cost allocation')	March 2014	Sets out a standard set of cost drivers for allocating 2013-14 costs between both the wholesale and retail and the household retail and non-household retail parts of the business.
'Setting price controls for 2015-20 – guidance for companies on producing default tariffs' (our 'default tariffs guidance')	April 2014	Further guidance on the data all companies should provide and the approach they should take in developing their default tariffs.

Document name	Publication date	Description/policy contents
'Service incentive mechanism (SIM) for 2015 onwards – conclusions' (our 'SIM conclusions paper')	April 2014	Summary of consultation responses received and resulting conclusions on the SIM for 2015 onwards.
'Setting price controls for 2015-20, Draft price control determination notice: technical appendix'	April 2014	Our approach to non-household retail price controls as part of the draft determinations for enhanced companies.
'Consultation on wholesale and retail charges for 2015-16 and charges scheme rules'	May 2014	Sets out our expectations for charging rules relevant to companies setting separate wholesale and retail charges in 2015-16, and our expectations for further changes in charging over the next five years and beyond.
'IN 14/14: 2014 price review – non-household customer engagement ahead of draft determination representations'	August 2014	Sets out our initial observations on incumbent companies' proposals for their non-household retail price controls ahead of our draft determinations.
'Setting price controls for 2015-20, Draft price control determination notice: technical appendix A5 – non-household retail' ('the non-household retail technical appendix to our August draft determinations')	August 2014	Restatement of our approach to household retail price controls including calculation of allowed retail household price control revenue as part of the August draft determinations.
'Final price control determination notice: policy chapter A6 – non-household retail costs and revenues'	December 2014	Price control policy summary published as part of our final determinations in December 2014.

Appendix B: Comparisons between the default tariff caps for metered water consumption

In this appendix, we set out a series of comparisons across all the 18 companies with non-household retail default tariff caps relating to metered water services. There are significant variations in the structure and levels of the default tariff caps set in 2014. While variation is not necessarily a concern in itself, it is not clear that all the differences in tariff structures are appropriate and that all the differences in tariff levels reflect differences in underlying costs.

We will publish further comparisons, including in relation to the default tariff caps for wastewater services, later in the price review.

B1 Metered water – water and sewerage companies

The table below shows the number of non-household metered water customers falling within each of the water and sewerage companies (WaSCs) appointed areas by the volume bands that define the default tariff caps.

Table B1: Numbers of metered water customers in 2017-18 (WaSCs)

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>0 to 0.5</td><td>99,751</td><td rowspan="11">157,225</td><td rowspan="7">168,406</td><td rowspan="3">51,901</td><td rowspan="9">89,005</td><td>131,981</td><td rowspan="11">68,696</td><td rowspan="3">37,622</td><td rowspan="11">110,491</td><td rowspan="11">92,622</td></tr>
<tr><td>0.5 to 0.75</td><td rowspan="5">4,811</td><td rowspan="2">17,375</td></tr>
<tr><td>0.75 to 1</td></tr>
<tr><td>1 to 2</td><td rowspan="3">4,593</td><td rowspan="3">23,074</td><td rowspan="3">3,144</td></tr>
<tr><td>2 to 4</td></tr>
<tr><td>4 to 5</td></tr>
<tr><td>5 to 10</td><td>845</td><td rowspan="3">837</td><td rowspan="3">5,023</td><td rowspan="4">413</td></tr>
<tr><td>10 to 15</td><td rowspan="3">446</td><td rowspan="4">901</td></tr>
<tr><td>15 to 20</td></tr>
<tr><td>20 to 25</td><td rowspan="3">285</td><td rowspan="2">123</td><td rowspan="2">822</td></tr>
<tr><td>25 to 50</td><td rowspan="9">291</td><td>39</td></tr>
<tr><td>50 to 100</td><td rowspan="8">190</td><td rowspan="8">200</td><td rowspan="3">93</td><td rowspan="4">306</td><td>13</td><td>22</td><td rowspan="4">112</td><td>54</td></tr>
<tr><td>100 to 150</td><td rowspan="7">13</td><td rowspan="3">18</td><td rowspan="3">16</td><td rowspan="3">31</td></tr>
<tr><td>150 to 175</td></tr>
<tr><td>175 to 250</td><td rowspan="5">37</td></tr>
<tr><td>250 to 350</td><td rowspan="4">21</td><td rowspan="4">2</td><td rowspan="2">1</td><td rowspan="4">29</td><td rowspan="2">10</td></tr>
<tr><td>350 to 500</td></tr>
<tr><td>500 to 1000</td><td rowspan="2">1</td><td>7</td></tr>
<tr><td>> 1000</td><td>1</td></tr>
</table>

Note: ANH = Anglian Water; UU = United Utilities; SVT = Severn Trent Water; SRN = Southern Water; NES = Northumbrian Water; TMS = Thames Water; SWT = South West Water; WSX = Wessex Water; YKY = Yorkshire Water; WSH = Dŵr Cymru.

Table B2 below shows how each company's default tariffs map to the default tariff cap bands.

Table B2: Allocation of default tariffs to volume bands (WaSCs)

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>0 to 0.5</td><td>Streamline Green (potable water) – (0.0Ml to 0.5Ml)</td><td rowspan="8">2 Up to 50Ml Water Metered</td><td rowspan="7">Band 2 – Water: 0-10 ml/a – metered</td><td rowspan="3">Standard 0-1Ml p.a. Water Metered</td><td rowspan="8">Cust type 03, Measured, Meas Water N std, Measured and Cust type 07, Measured, Meas Water S std, Measured</td><td>[0 – 500] [0 – 500m^3] [water] [metered]</td><td rowspan="8">Standard Measured Water</td><td rowspan="3">M-W-0; 0-1 Ml water metered</td><td rowspan="8">Tariff band 1 ≤50 Ml/a water metered</td><td rowspan="8">Potable Water < 50Ml (Non-household)</td></tr>
<tr><td>0.5 to 0.75</td><td rowspan="5">Streamline Orange (potable water) – (0.5Ml to 5.0Ml)</td><td rowspan="2">[500 – 1,000] [500 – 1,000m^3] [water] [metered]</td></tr>
<tr><td>0.75 to 1</td></tr>
<tr><td>1 to 2</td><td rowspan="3">Standard 1-5Ml p.a. Water Metered</td><td rowspan="3">[1,000 – 5,000] [1,000 – 5,000m^3] [water] [metered]</td><td rowspan="3">M-W-1; 1-5Ml water metered</td></tr>
<tr><td>2 to 4</td></tr>
<tr><td>4 to 5</td></tr>
<tr><td>5 to 10</td><td>Streamline Blue (potable water) – (5.0Ml to 10.0Ml)</td><td rowspan="2">Standard 5-20Ml p.a. Water Metered</td><td rowspan="2">[5,000 – 20,000] [5,000 – 20,000m^3] [water] [metered]</td><td rowspan="2">M-W-5; 5-25Ml water metered</td></tr>
<tr><td>10 to 15</td><td>Profile</td><td>Band 3 –</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>15 to 20</td><td rowspan="2">(potable water) – (10.0Ml to 25.0Ml)</td><td rowspan="3"></td><td rowspan="3">Water: 10-50 ml/a – metered</td><td></td><td></td><td></td><td rowspan="3"></td><td rowspan="2"></td><td rowspan="3"></td><td rowspan="3"></td></tr>
<tr><td>20 to 25</td><td rowspan="3">Standard 20-100Ml p.a. Water Metered</td><td rowspan="2">Cust type 04, Measured, Meas Water N f20, Measured and Cust type 08, Measured, Meas Water S f20, Measured</td><td rowspan="2">[20,000 – 50,000] [20,000 – 50,000m³] [water] [metered]</td></tr>
<tr><td>25 to 50</td><td rowspan="6">Profile Plus (potable water) – (25.0Ml +)</td><td>M-W-25; 25-50Ml water metered</td></tr>
<tr><td>50 to 100</td><td rowspan="5">3 > 50Ml water metered</td><td rowspan="5">Band 4 – Water: 50+ ml/a – metered</td><td rowspan="3">Cust type 05, Measured, Meas Water N fx, Measured and Cust type 09, Measured, Meas Water S fx, Measured</td><td rowspan="4">[50,000 – 250,000] [50,000 – 250,000m³] [water] [metered]</td><td>Large and Special User 50-100ML Water</td><td>M-W-50; 50-100Ml water metered</td><td rowspan="4">Tariff band 2 > 50 ≤ 250 Ml/a water metered</td><td>Water Large User 50Ml-99Ml (Measured)</td></tr>
<tr><td>100 to 150</td><td rowspan="4">Standard Over 100Ml p.a. Water Metered</td><td rowspan="3">Large and Special User 100-250ML Water</td><td rowspan="3">M-W-100; 100-250Ml water metered</td><td rowspan="3">Water Large User 100Ml-249Ml (Measured)</td></tr>
<tr><td>150 to 175</td></tr>
<tr><td>175 to 250</td><td rowspan="2">Cust type 06, Measured, Meas Water N f+,</td></tr>
<tr><td>250 to 350</td><td>[250,000 +] [250,000 +m³] [water]</td><td>Large and Special User</td><td>M-W-250; 250-500Ml</td><td>Tariff band 3 > 250 Ml/a</td><td>Water Large User 250Ml-499Ml</td></tr>
</table>

Volume Band (Ml)	ANH	UU	SVT	SRN	NES	TMS	SWT	WSX	YKY	WSH
350 to 500					Measured and Cust type 10, Measured, Meas Water S f+, Measured	[metered]	250+ML Water	water metered	water metered	(Measured)
500 to 1000								M-W-500; >500Ml water metered		Water Large User 500Ml-1000Ml (Measured)
> 1000										Water Large User >1000 (Measured)

Table B1 shows that the large majority (94%) of customers fall within the lowest default tariff cap volume band chosen by each company. However, companies have selected markedly different volume ranges for their lowest band and different numbers of bands. For example, Anglian Water and Thames Water have adopted a band between 0 and 0.5 Ml a year whereas United Utilities, South West Water, Yorkshire Water and Dŵr Cymru have a lowest band, which extends up to 50Ml a year. United Utilities has only two customer types for metered water whereas Wessex Water has eight customer types.

Table B3 shows the average gross margins published as part of our final determinations in December 2014.

Table B3: Average gross margin (£ per customer) for metered water supplies in 2017-18 (WaSCs)

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>0 to 0.5</td><td>56.82</td><td rowspan="11">66.38</td><td rowspan="7">69.28</td><td rowspan="3">36.25</td><td rowspan="9">60.99</td><td rowspan="9">51.19</td><td>30.76</td><td rowspan="11">35.82</td><td rowspan="3">31.01</td><td rowspan="11">48.34</td><td rowspan="11">41.30</td></tr>
<tr><td>0.5 to 0.75</td><td rowspan="5">155.53</td><td rowspan="2">80.21</td></tr>
<tr><td>0.75 to 1</td></tr>
<tr><td>1 to 2</td><td rowspan="3">157.07</td><td rowspan="3">114.55</td><td rowspan="3">116.29</td></tr>
<tr><td>2 to 4</td></tr>
<tr><td>4 to 5</td></tr>
<tr><td>5 to 10</td><td>595.85</td><td rowspan="3">408.89</td><td rowspan="3">317.34</td><td rowspan="4">396.02</td></tr>
<tr><td>10 to 15</td><td rowspan="3">806.64</td><td rowspan="4">522.76</td></tr>
<tr><td>15 to 20</td></tr>
<tr><td>20 to 25</td><td rowspan="3">652.83</td><td rowspan="2">1,623.23</td><td rowspan="2">1,226.55</td><td rowspan="2">843.30</td></tr>
<tr><td>25 to 50</td><td rowspan="9">1,500.50</td><td>1,131.43</td></tr>
<tr><td>50 to 100</td><td rowspan="8">12,124.09</td><td rowspan="8">2,203.76</td><td rowspan="3">4,058.15</td><td rowspan="3">4,309.38</td><td rowspan="4">2,271.34</td><td>2,733.02</td><td>2,503.42</td><td rowspan="4">1,361.32</td><td>4,910.82</td></tr>
<tr><td>100 to 150</td><td rowspan="7">4,107.72</td><td rowspan="3">5,755.35</td><td rowspan="3">3,843.69</td><td rowspan="3">7,031.29</td></tr>
<tr><td>150 to 175</td></tr>
<tr><td>175 to 250</td><td rowspan="5">6,527.40</td><td rowspan="5">5,675.01</td></tr>
<tr><td>250 to 350</td><td rowspan="4">8,140.03</td><td rowspan="4">12,790.61</td><td rowspan="2">5,206.26</td><td rowspan="4">5,561.87</td><td rowspan="2">14,564.12</td></tr>
<tr><td>350 to 500</td></tr>
<tr><td>500 to 1000</td><td rowspan="2">10,127.54</td><td>22,636.58</td></tr>
<tr><td>> 1000</td><td>41,132.26</td></tr>
</table>

The table shows some marked differences between the gross margins each company could earn for similar levels of consumption. Some of these differences occur because of the different volume bands that companies have adopted. Others may arise from differences in the approach to cost allocation that companies have adopted.

There are significant variations between companies – although these impact on the volume bands covering a relatively small number of customers. For the default tariff caps applying to large customers with volumes in excess of 50 Ml a year, Severn Trent has a gross margin of £2,204 for each customer, whereas United Utilities has a margin of £12,124 for each customer.

For the default tariff caps applying to very large customers with volumes in excess of 250 Ml a year, Yorkshire Water has a gross margin of £5,562, whereas Dŵr Cymru has margins ranging from £14,564 to £41,132 for each customer.

For the default tariff caps applying to the smallest customers with volumes up to 0.5 Ml per year, Thames Water has a gross margin of £31 for each customer whereas Anglian Water has a gross margin of £57 for each customer.

Table B4 shows the relative contribution of the two components which together form the gross margin, the allowed retail margin and the allowed retail cost. Dŵr Cymru is a relative outlier because of the lower net margins allowed for non-contestable customers within Dŵr Cymru.

Table B4: Net margins and retail costs as a proportion of the gross margins (WaSCs)

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>0 to 0.5</td><td>40:60</td><td rowspan="11">35:65</td><td rowspan="7">33:67</td><td rowspan="3">36:64</td><td rowspan="9">49:51</td><td rowspan="9">53:47</td><td>15:85</td><td rowspan="11">54:46</td><td rowspan="3">37:63</td><td rowspan="11">45:55</td><td rowspan="11">16:84</td></tr>
<tr><td>0.5 to 0.75</td><td rowspan="5">41:59</td><td rowspan="2">27:73</td></tr>
<tr><td>0.75 to 1</td></tr>
<tr><td>1 to 2</td><td rowspan="3">48:52</td><td rowspan="3">51:49</td><td rowspan="3">66:34</td></tr>
<tr><td>2 to 4</td></tr>
<tr><td>4 to 5</td></tr>
<tr><td>5 to 10</td><td>37:63</td><td rowspan="3">51:49</td><td rowspan="3">74:26</td><td rowspan="4">61:39</td></tr>
<tr><td>10 to 15</td><td rowspan="3">42:58</td><td rowspan="4">81:19</td></tr>
<tr><td>15 to 20</td></tr>
<tr><td>20 to 25</td><td rowspan="3">51:49</td><td rowspan="2">37:63</td><td rowspan="2">46:54</td><td rowspan="2">86:14</td></tr>
<tr><td>25 to 50</td><td rowspan="9">64:36</td><td>69:31</td></tr>
<tr><td>50 to 100</td><td rowspan="8">59:41</td><td rowspan="8">95:5</td><td rowspan="3">39:61</td><td rowspan="3">43:57</td><td rowspan="4">91:9</td><td>72:28</td><td>62:38</td><td rowspan="4">97:3</td><td>54:46</td></tr>
<tr><td>100 to 150</td><td rowspan="7">53:47</td><td rowspan="3">79:21</td><td rowspan="3">73:27</td><td rowspan="3">55:45</td></tr>
<tr><td>150 to 175</td></tr>
<tr><td>175 to 250</td><td rowspan="5">62:38</td><td rowspan="5">56:44</td></tr>
<tr><td>250 to 350</td><td rowspan="4">92:8</td><td rowspan="4">85:15</td><td rowspan="2">83:17</td><td rowspan="4">99:1</td><td rowspan="2">56:44</td></tr>
<tr><td>350 to 500</td></tr>
<tr><td>500 to 1000</td><td rowspan="2">91:9</td><td>56:44</td></tr>
<tr><td>> 1000</td><td>57:43</td></tr>
<tr><td>Company</td><td>42:58</td><td>39:61</td><td>37:63</td><td>41:59</td><td colspan="2">51:49</td><td>36:64</td><td>61:39</td><td>51:49</td><td>48:52</td><td>24:76</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>Average</td><td></td><td></td><td></td><td></td><td colspan="2"></td><td></td><td></td><td></td><td></td><td></td></tr>
</table>

Tables B5 and B6 provide further detail on the two components of gross margin – net margins and retail costs. They illustrate there is significant variation between companies in the way the components of the gross margin have been allocated to individual tariff bands by different companies.

Table B5: Net margin (%) for metered water supplies in 2017-18 (WaSCs)

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>0 to 0.5</td><td>4.6%</td><td rowspan="11">2.5%</td><td rowspan="7">3.1%</td><td rowspan="3">6.5%</td><td rowspan="9">3.9%</td><td rowspan="9">3.3%</td><td>2.5%</td><td rowspan="11">2.7%</td><td rowspan="3">3.6%</td><td rowspan="11">2.8%</td><td rowspan="11">1.0%</td></tr>
<tr><td>0.5 to 0.75</td><td rowspan="5">2.3%</td><td rowspan="2">2.5%</td></tr>
<tr><td>0.75 to 1</td></tr>
<tr><td>1 to 2</td><td rowspan="3">2.9%</td><td rowspan="3">2.5%</td><td rowspan="3">1.7%</td></tr>
<tr><td>2 to 4</td></tr>
<tr><td>4 to 5</td></tr>
<tr><td>5 to 10</td><td>2.8%</td><td rowspan="3">2.5%</td><td rowspan="3">2.5%</td><td rowspan="4">1.4%</td></tr>
<tr><td>10 to 15</td><td rowspan="3">1.9%</td><td rowspan="4">1.5%</td></tr>
<tr><td>15 to 20</td></tr>
<tr><td>20 to 25</td><td rowspan="3">1.4%</td><td rowspan="2">1.8%</td><td rowspan="2">1.1%</td><td rowspan="2">2.5%</td></tr>
<tr><td>25 to 50</td><td rowspan="3">0.9%</td><td>1.1%</td></tr>
<tr><td>50 to 100</td><td rowspan="2">2.5%</td><td rowspan="2">1.4%</td><td rowspan="2">1.5%</td><td rowspan="2">1.3%</td><td rowspan="2">2.5%</td><td>1.8%</td><td>1.1%</td><td rowspan="2">1.3%</td><td>2.5%</td></tr>
<tr><td>100 to 150</td><td>0.7%</td><td>1.8%</td><td>0.9%</td><td>2.5%</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>150 to 175</td><td rowspan="6"></td><td rowspan="6"></td><td rowspan="6"></td><td rowspan="6"></td><td></td><td></td><td rowspan="2"></td><td rowspan="2"></td><td rowspan="2"></td><td rowspan="2"></td><td rowspan="2"></td></tr>
<tr><td>175 to 250</td><td rowspan="5">0.8%</td><td rowspan="5">0.8%</td></tr>
<tr><td>250 to 350</td><td rowspan="4">2.5%</td><td rowspan="4">1.9%</td><td rowspan="2">0.8%</td><td rowspan="4">1.3%</td><td rowspan="2">2.5%</td></tr>
<tr><td>350 to 500</td></tr>
<tr><td>500 to 1000</td><td rowspan="2">0.7%</td><td>2.5%</td></tr>
<tr><td>> 1000</td><td>2.5%</td></tr>
</table>

Table B6: Retail costs (£ per customer) for metered water supplies in 2017-18 (WaSCs)

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>0 to 0.5</td><td>34.32</td><td rowspan="11">43.25</td><td rowspan="7">46.62</td><td rowspan="3">23.30</td><td rowspan="9">31.37</td><td rowspan="9">24.09</td><td>26.16</td><td rowspan="11">16.51</td><td rowspan="3">19.40</td><td rowspan="11">26.74</td><td rowspan="11">34.71</td></tr>
<tr><td>0.5 to 0.75</td><td rowspan="5">92.00</td><td rowspan="2">58.72</td></tr>
<tr><td>0.75 to 1</td></tr>
<tr><td>1 to 2</td><td rowspan="3">81.43</td><td rowspan="3">55.69</td><td rowspan="3">39.84</td></tr>
<tr><td>2 to 4</td></tr>
<tr><td>4 to 5</td></tr>
<tr><td>5 to 10</td><td>372.54</td><td rowspan="3">201.87</td><td rowspan="3">83.81</td><td rowspan="4">156.02</td></tr>
<tr><td>10 to 15</td><td rowspan="3">467.08</td><td rowspan="4">98.26</td></tr>
<tr><td>15 to 20</td></tr>
<tr><td>20 to 25</td><td rowspan="2">320.85</td><td rowspan="2">1,019.14</td><td rowspan="2">658.93</td><td rowspan="2">121.85</td></tr>
<tr><td>25 to 50</td><td>537.56</td><td>349.06</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>ANH</th><th>UU</th><th>SVT</th><th>SRN</th><th>NES (N)</th><th>NES (S)</th><th>TMS</th><th>SWT</th><th>WSX</th><th>YKY</th><th>WSH</th></tr>
<tr><td>50 to 100</td><td rowspan="8"></td><td rowspan="8">4,929.20</td><td rowspan="8">117.04</td><td></td><td rowspan="3">2,465.76</td><td rowspan="3">2,461.88</td><td rowspan="4">215.55</td><td>758.45</td><td>948.82</td><td rowspan="4">42.67</td><td>2,262.43</td></tr>
<tr><td>100 to 150</td><td rowspan="7">1,922.16</td><td rowspan="3">1,205.09</td><td rowspan="3">1,021.01</td><td rowspan="3">3,163.44</td></tr>
<tr><td>150 to 175</td></tr>
<tr><td>175 to 250</td><td rowspan="5">2,496.44</td><td rowspan="5">2,478.54</td></tr>
<tr><td>250 to 350</td><td rowspan="4">659.19</td><td rowspan="4">1,971.97</td><td rowspan="2">907.57</td><td rowspan="4">47.28</td><td rowspan="2">6,393.84</td></tr>
<tr><td>350 to 500</td></tr>
<tr><td>500 to 1000</td><td rowspan="2">907.57</td><td>9,947.68</td></tr>
<tr><td>> 1000</td><td>17,838.57</td></tr>
</table>

B2 Metered water – water only companies

Tables B7 to B12 provide the equivalent information as in tables B1 to B6 but for metered water customers of the water only companies (WoCs) rather than WaSCs. They show similar trends and issues as discussed in relation to tables B1 to B6.

Table B7: Numbers of metered water customers in 2017-18 (WoCs)

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>0 to 0.5</td><td rowspan="4">60,256</td><td rowspan="3">26,249</td><td rowspan="4">7,536</td><td rowspan="4">14,244</td><td rowspan="2">13,213</td><td rowspan="4">13,327</td><td rowspan="4">53,034</td><td rowspan="4">27,640</td><td rowspan="4">9,315</td></tr>
<tr><td>0.5 to 0.75</td></tr>
<tr><td>0.75 to 1</td><td rowspan="2">1,317</td></tr>
<tr><td>1 to 2</td><td>2,807</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>2 to 4</td><td rowspan="15"></td><td rowspan="2"></td><td rowspan="7"></td><td rowspan="3"></td><td>428</td><td rowspan="3"></td><td rowspan="2"></td><td rowspan="7"></td><td rowspan="9"></td></tr>
<tr><td>4 to 5</td><td rowspan="2">261</td></tr>
<tr><td>5 to 10</td><td rowspan="2">387</td><td>613</td></tr>
<tr><td>10 to 15</td><td rowspan="4">153</td><td rowspan="4">80</td><td rowspan="4">55</td><td rowspan="4">362</td></tr>
<tr><td>15 to 20</td><td rowspan="3">84</td></tr>
<tr><td>20 to 25</td></tr>
<tr><td>25 to 50</td></tr>
<tr><td>50 to 100</td><td>25</td><td rowspan="4">12</td><td rowspan="8">28</td><td rowspan="8">4</td><td rowspan="8">4</td><td rowspan="4">41</td><td rowspan="5">27</td></tr>
<tr><td>100 to 150</td><td rowspan="3">14</td></tr>
<tr><td>150 to 175</td><td rowspan="6">2</td></tr>
<tr><td>175 to 250</td></tr>
<tr><td>250 to 350</td><td rowspan="4">1</td><td rowspan="4">1</td><td rowspan="4">1</td></tr>
<tr><td>350 to 500</td><td rowspan="3">3</td></tr>
<tr><td>500 to 1000</td></tr>
<tr><td>> 1000</td></tr>
</table>

Note: AFW = Affinity Water; BRL = Bristol Water; DVW = Dee Valley Water; PRT = Portsmouth Water; SBW = Bournemouth water; SES = Sutton & East Surrey Water; SEW = South East Water; SST = South Staffordshire Water; CAM = Cambridge Water.

Table B7 has been compiled by mapping company customer types to volume bands. The allocation assumptions are detailed in table B8 below.

Table B8: Allocation of default tariffs to volume bands (WoCs)

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>0 to 0.5</td><td rowspan="13">Affinity Water Measured Half Yearly, no volume band, water, metered & Affinity Water Measured Monthly, no volume band, water, metered</td><td rowspan="3">Band G – 0-1Ml</td><td rowspan="11">Tariff band 02 – Measured less than 50Ml</td><td rowspan="7">Water Measured Non-Household < 10Ml</td><td rowspan="2">Domestic Commercials 0 to 750 m³/a Water Metered</td><td rowspan="7">Northern area standard user metered & Southern area standard user metered</td><td rowspan="6">[0-5Mla] [water] [metered]</td><td rowspan="11">Measured <50 Ml/yr – South Staffordshire Region</td><td rowspan="13">Measured <150 Ml/yr – Cambridge region</td></tr>
<tr><td>0.5 to 0.75</td></tr>
<tr><td>0.75 to 1</td><td rowspan="2">Small Commercials 750 to 2000 m³/a Water Metered</td></tr>
<tr><td>1 to 2</td><td rowspan="3">Band F – 1-5Ml</td></tr>
<tr><td>2 to 4</td><td>Small Medium Commercials 2000 to 4000 m³/a Water Metered</td></tr>
<tr><td>4 to 5</td><td rowspan="2">Large Medium Commercials 4000 to 10,000 m³/a Water Metered</td></tr>
<tr><td>5 to 10</td><td rowspan="2">Band E 5-15Ml</td><td>[5-10Mla] [water] [metered]</td></tr>
<tr><td>10 to 15</td><td rowspan="4">Water Measured Non-Household > 10Ml and < 50Ml</td><td rowspan="4">High Commercials 10,000 to 50,000 m³/a Water Metered</td><td rowspan="4">Northern area mid user metered & Southern area mid user metered</td><td rowspan="4">[10-50Mla] [water] [metered]</td></tr>
<tr><td>15 to 20</td><td rowspan="3">Band D – 15-50 Ml</td></tr>
<tr><td>20 to 25</td></tr>
<tr><td>25 to 50</td></tr>
<tr><td>50 to 100</td><td>Band C – 50-100 Ml</td><td rowspan="2">Tariff band 05 – Measured 50ML –</td><td rowspan="2">Water Measured Non-Household</td><td rowspan="2">Very High Commercials>50,000 m³/a Water Metered</td><td rowspan="2">Northern area high user metered</td><td rowspan="2">[50-250Mla [water] [metered]</td><td rowspan="2">Medium User >=50 Ml/yr – South Staffordshire</td></tr>
<tr><td>100 to 150</td><td>Band B</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>150 to 175</td><td rowspan="6"></td><td rowspan="2">– 100-250Ml</td><td rowspan="2">250 ML</td><td rowspan="6">> 50Ml</td><td rowspan="6"></td><td rowspan="6">& Southern area high user metered</td><td rowspan="2"></td><td rowspan="3">Region & Large User Up to 350 Ml/yr – South Staffordshire Region</td><td rowspan="6">Measured >=150 Ml/yr – Cambridge region</td></tr>
<tr><td>175 to 250</td></tr>
<tr><td>250 to 350</td><td rowspan="4">Band A – 250Ml+</td><td rowspan="4">Tariff band 04 – Large user</td><td rowspan="4">[over 250Mla] [water] [metered/unmetered]</td></tr>
<tr><td>350 to 500</td><td rowspan="3">Large User Over 350 Ml/yr – South Staffordshire Region</td></tr>
<tr><td>500 to 1000</td></tr>
<tr><td>> 1000</td></tr>
</table>

Table B9: Average gross margin (£ per customer) for metered water supplies in 2017-18 (WoCs)

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>0 to 0.5</td><td rowspan="10">63.03 (Half yearly billing) 464.02 (Monthly billing)</td><td rowspan="3">33.81</td><td rowspan="10">38.11</td><td rowspan="7">29.38</td><td rowspan="2">22.04</td><td rowspan="7">49.12</td><td rowspan="6">52.64</td><td rowspan="10">63.80</td><td rowspan="10">50.74</td></tr>
<tr><td>0.5 to 0.75</td></tr>
<tr><td>0.75 to 1</td><td rowspan="2">44.70</td></tr>
<tr><td>1 to 2</td><td rowspan="3">87.80</td></tr>
<tr><td>2 to 4</td><td>163.67</td></tr>
<tr><td>4 to 5</td><td rowspan="2">465.42</td></tr>
<tr><td>5 to 10</td><td rowspan="2">386.85</td><td>305.75</td></tr>
<tr><td>10 to 15</td><td rowspan="3">397.27</td><td rowspan="3">903.86</td><td rowspan="3">1,018.54</td><td rowspan="3">670.15</td></tr>
<tr><td>15 to 20</td><td rowspan="2">1,098.35</td></tr>
<tr><td>20 to 25</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>25 to 50</td><td rowspan="9"></td><td></td><td></td><td></td><td></td><td></td><td></td><td></td><td rowspan="3"></td></tr>
<tr><td>50 to 100</td><td>2,343.52</td><td rowspan="4">2,631.60</td><td rowspan="8">1,986.76</td><td rowspan="8">2,097.62</td><td rowspan="8">3,564.23</td><td rowspan="4">2,942.16</td><td rowspan="5">2,383.00</td></tr>
<tr><td>100 to 150</td><td rowspan="3">4,293.93</td></tr>
<tr><td>150 to 175</td><td rowspan="6">8,126.66</td></tr>
<tr><td>175 to 250</td></tr>
<tr><td>250 to 350</td><td rowspan="4">9,028.38</td><td rowspan="4">8,613.71</td><td rowspan="4">13,648.00</td></tr>
<tr><td>350 to 500</td><td rowspan="3">14,361.35</td></tr>
<tr><td>500 to 1000</td></tr>
<tr><td>> 1000</td></tr>
</table>

Table B10: Net margins and retail costs as a proportion of the gross margins

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>0 to 0.5</td><td rowspan="8">9:91 (Half yearly billing) 72:28 (Monthly billing)</td><td rowspan="3">28:72</td><td rowspan="8">17:83</td><td rowspan="7">31:69</td><td rowspan="2">9:91</td><td rowspan="7">34:66</td><td rowspan="6">29:71</td><td rowspan="8">20:80</td><td rowspan="8">33:67</td></tr>
<tr><td>0.5 to 0.75</td></tr>
<tr><td>0.75 to 1</td><td rowspan="2">56:44</td></tr>
<tr><td>1 to 2</td><td rowspan="3">52:48</td></tr>
<tr><td>2 to 4</td><td>85:15</td></tr>
<tr><td>4 to 5</td><td rowspan="2">67:33</td></tr>
<tr><td>5 to 10</td><td rowspan="2">51:49</td><td>77:23</td></tr>
<tr><td>10 to 15</td><td>90:10</td><td>80:20</td><td>48:52</td><td>89:11</td></tr>
</table>

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>15 to 20</td><td rowspan="11"></td><td rowspan="3">55:45</td><td rowspan="3"></td><td rowspan="3"></td><td rowspan="3"></td><td rowspan="3"></td><td rowspan="3"></td><td rowspan="3"></td><td rowspan="5"></td></tr>
<tr><td>20 to 25</td></tr>
<tr><td>25 to 50</td></tr>
<tr><td>50 to 100</td><td>68:32</td><td rowspan="4">99:1</td><td rowspan="8">98:2</td><td rowspan="8">64:36</td><td rowspan="8">83:17</td><td rowspan="4">95:5</td><td rowspan="5">96:4</td></tr>
<tr><td>100 to 150</td><td rowspan="3">78:22</td></tr>
<tr><td>150 to 175</td><td rowspan="6">99:1</td></tr>
<tr><td>175 to 250</td></tr>
<tr><td>250 to 350</td><td rowspan="4">81:19</td><td rowspan="4">100:0</td><td rowspan="4">99:1</td></tr>
<tr><td>350 to 500</td><td rowspan="3">99:1</td></tr>
<tr><td>500 to 1000</td></tr>
<tr><td>> 1000</td></tr>
<tr><td>Company Average</td><td>30:70</td><td>39:61</td><td>26:74</td><td>44:56</td><td>48:52</td><td>36:64</td><td>38:62</td><td colspan="2">26:74</td></tr>
</table>

Table B11: Net margin (%) for metered water supplies in 2017-18 (WoCs)

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>0 to 0.5</td><td rowspan="19">2.4% (Half yearly billing) 2.6% (Monthly billing)</td><td rowspan="3">3.80%</td><td rowspan="11">1.00%</td><td rowspan="7">2.40%</td><td rowspan="2">1.40%</td><td rowspan="7">2.50%</td><td rowspan="6">2.80%</td><td rowspan="11">2.50%</td><td rowspan="13">2.50%</td></tr>
<tr><td>0.5 to 0.75</td></tr>
<tr><td>0.75 to 1</td><td rowspan="2">1.90%</td></tr>
<tr><td>1 to 2</td><td rowspan="3">1.80%</td></tr>
<tr><td>2 to 4</td><td>4.30%</td></tr>
<tr><td>4 to 5</td><td rowspan="2">4.30%</td></tr>
<tr><td>5 to 10</td><td rowspan="2">2.10%</td><td>2.30%</td></tr>
<tr><td>10 to 15</td><td rowspan="4">2.80%</td><td rowspan="4">3.80%</td><td rowspan="4">2.50%</td><td rowspan="4">2.30%</td></tr>
<tr><td>15 to 20</td><td rowspan="3">2.10%</td></tr>
<tr><td>20 to 25</td></tr>
<tr><td>25 to 50</td></tr>
<tr><td>50 to 100</td><td>2.00%</td><td rowspan="4">2.50%</td><td rowspan="8">2.50%</td><td rowspan="8">1.70%</td><td rowspan="8">2.50%</td><td rowspan="4">2.30%</td><td rowspan="5">2.50%</td></tr>
<tr><td>100 to 150</td><td rowspan="3">2.00%</td></tr>
<tr><td>150 to 175</td><td rowspan="6">2.50%</td></tr>
<tr><td>175 to 250</td></tr>
<tr><td>250 to 350</td><td rowspan="4">2.10%</td><td rowspan="4">2.50%</td><td rowspan="4">2.30%</td></tr>
<tr><td>350 to 500</td><td rowspan="3">2.50%</td></tr>
<tr><td>500 to 1000</td></tr>
<tr><td>> 1000</td></tr>
</table>

Table B12: Retail costs (£ per customer) for metered water supplies in 2017-18 (WoCs)

<table>
<tr><th>Volume Band (Ml)</th><th>AFW</th><th>BRL</th><th>DVW</th><th>PRT</th><th>SBW</th><th>SES</th><th>SEW</th><th>SST</th><th>CAM</th></tr>
<tr><td>0 to 0.5</td><td rowspan="19">49.96 (Half yearly billing) 175.84 (Monthly billing)</td><td rowspan="3">24.46</td><td rowspan="11">31.62</td><td rowspan="7">20.22</td><td rowspan="2">20.09</td><td rowspan="7">32.38</td><td rowspan="6">37.13</td><td rowspan="11">50.78</td><td rowspan="13">34.01</td></tr>
<tr><td>0.5 to 0.75</td></tr>
<tr><td>0.75 to 1</td><td rowspan="2">19.78</td></tr>
<tr><td>1 to 2</td><td rowspan="3">42.48</td></tr>
<tr><td>2 to 4</td><td>25.29</td></tr>
<tr><td>4 to 5</td><td rowspan="2">154.75</td></tr>
<tr><td>5 to 10</td><td rowspan="2">187.83</td><td>71.80</td></tr>
<tr><td>10 to 15</td><td rowspan="4">40.35</td><td rowspan="4">182.65</td><td rowspan="4">532.17</td><td rowspan="4">76.59</td></tr>
<tr><td>15 to 20</td><td rowspan="3">496.94</td></tr>
<tr><td>20 to 25</td></tr>
<tr><td>25 to 50</td></tr>
<tr><td>50 to 100</td><td>738.41</td><td rowspan="4">31.56</td><td rowspan="8">36.74</td><td rowspan="8">764.27</td><td rowspan="8">607.18</td><td rowspan="4">146.77</td><td rowspan="5">89.29</td></tr>
<tr><td>100 to 150</td><td rowspan="3">924.79</td></tr>
<tr><td>150 to 175</td><td rowspan="6">42.12</td></tr>
<tr><td>175 to 250</td></tr>
<tr><td>250 to 350</td><td rowspan="4">1,731.02</td><td rowspan="4">29.90</td><td rowspan="4">136.76</td></tr>
<tr><td>350 to 500</td><td rowspan="3">89.29</td></tr>
<tr><td>500 to 1000</td></tr>
<tr><td>> 1000</td></tr>
</table>

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

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