

Phil Griffiths
Ofwat
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11th December 2015

Dear Sirs,

Consultation on the review of non-household retail price controls

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

We believe that this review should focus only on non-household price controls, in line with Ofwat's original intentions.

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 existing controls, consistent with the expectations set out in our final determinations?

We think a key objective of the initial 2-year period was to allow new information about costs and margins to emerge so that where there is new evidence to support it, the costs and margins should be capable of being re-allocated. This should allow default tariffs to reflect costs better and should improve the economic efficiency of the retail charges against which new entrants are competing. We further note that if the proposals in Q4. below are taken forwards this would seem to necessitate re-allocations, since if companies are to increase or decrease the number of default tariffs they operate, of necessity they would surely need to review their new structures for default tariffs and re-allocate cost and margins.

We are content that the aggregate levels of costs and margins should stay the same in because it should afford customers the same level of price protection as in the 2015 price limits.

Companies that have reduced costs between 2014 and now, should not have the aggregate level of costs and margins in their default tariffs reduced as this would reduce efficiency incentives. Instead, the benefit of efficiency gains should continue until either competition develops sufficiently strongly to compete them away, or at the end of the price control period (2020) when default tariffs can be reviewed or reset, as required.

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

We think that the only way to achieve the objective of full transparency is for companies to disclose a list of tariffs that they include within each default tariff category. This of course represents an additional information requirement on companies, but it is information that companies should have readily available and it could for example be included as an annex to published charges schemes.

In our case however, our default tariffs are based on whether customers are measured, unmeasured, assessed or special agreement customers and within the measured category, whether they are larger users billed on a monthly basis or smaller customers billed on a half-yearly basis. We think it already reasonably straightforward for customers or competitors to see in which default tariff category they belong. (We accept that this may not be the case for other companies, or for wastewater default tariffs.)

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?

We think that as part of the review it is fair to ask companies to consider carefully the number and structures of default tariffs they offer, taking into account comparisons with other companies as well as other evidence they have collected since last price review.

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?

We are comfortable with the idea that we provide our cost and margin allocations to Ofwat, along with details of the activity levels and drivers that we have used to reach the allocations as it seems that this is information reasonably required by Ofwat to make its determinations.

However we do not think it fair that this information be published as it would give potential competitors an unfair information advantage. It seems to us unreasonable to expect undertakers to publish detailed breakdowns of the costs and margins underpinning prices when this would not be required of new entrants.

The second suggestion is far more palatable; that we engage expert consultants to review our default tariffs and report on their consistency with competition law.

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?

If companies do not wish to alter their default tariff caps, because there is not sufficient evidence to do so, or because the proposals in Q4 are not to be carried forward, then it seems reasonable to allow this. Ofwat could have confidence in retention of existing default tariff caps through the expert review suggested in Q5, and by the requirements for Board assurance and customer engagement set out on p17 of the consultation.

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?

We agree that a three-year duration is the most appropriate duration for the next non-household retail price control. This is advantageous because it gives sufficient time to take into account information about the operation of competition from its 2017 introduction. A shorter duration might not allow this.

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?



The timetable appears to be reasonable and acceptable to us although it would be of assistance if Ofwat could look at ways to bring forwards the deadline for methodology and information requirements from April.

Yours sincerely

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

Martin Hall
Senior Regulatory Economist

