



Note of the access pricing working group meeting held 21 March 2014

1. Introduction

Ofwat explained the context for the development of a future access pricing framework. Although the government does not envisage implementing the upstream reforms until 2019 and beyond, work needs to commence in advance to ensure an appropriate level of readiness. In developing final rules, Ofwat will have regard to any guidance produced by the Secretary of State and Welsh Ministers.

2. Main issues

Ofwat set out seven key issues to be addressed through the access pricing workstream:

- preventing monopoly abuse;
- selecting the right level of cost information;
- de-averaging;
- the RCV discount;
- helping the environment;
- interactions with the 2014 price review; and
- interactions with the Open Water programme.

The working group provided views of further key considerations. These included how to treat the recovery of expenditure associated with environmental schemes that provide a common benefit.

It was also suggested that there may be benefit in explicitly considering asset stranding at the principle, rather than the detail, level.

It was also suggested that there may be benefit in directly testing all access pricing proposals against a suitable competition test, to help ensure proposals remain compliant with the law.

3. Other sectors

Ofwat requested views from the working group whether there were any precedents from other sectors that might be particularly relevant.

Working group members posed that there may be some read-across from telecom sector, as in telecoms the issue of a wide number of different services has been addressed.

It was noted that in electricity a third party consultant was used to help develop a standardised methodology. Using the third party helped mitigate the risk of collusion. However, it was also noted that in the water industry the companies are vertically integrated, potentially giving a greater incentive for anti-competitive access pricing, and so further assurance may be required.

It was noted that long-run incremental costs (LRICs) have been widely used.

It was suggested that the publication of distributed stand-alone costs (DSACs) and DLRICs can help provide signals to entrants, even if actual pricing is allowed to vary from these approaches.

4. Bulk supplies

The relative pros and cons were discussed of considering the charging approach for bulk supplies alongside access pricing. It was recognised that there may be many overlapping policy areas; however, the longer term work on access pricing should not restrict development of bulk supply charging policy.

5. Retail access

The working group was asked whether it could envisage any situation where the retail access price would not simply be the wholesale charge. No clear circumstance was identified, although, it was recognised that there may be costs of competition to the wholesaler, which may need to be reflected in the wholesale charge(s).

6. Actions and next steps

Ofwat is in the process of developing a work plan to be discussed internally within Ofwat.

The working group provided views on which issues need to be addressed upfront. These included the following.

- What should the overall assessment criteria be for an effective framework?
- How should the RCV discount be treated?
- What are the separable services?
- Which services/parts of the value chain would require geographic specific pricing?

- How should environmental expenditure/other common costs be treated?