

Consultation: Bulk charges for NAV's

South East Water response

DATE

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Contents

1.	Introduction	4
2.	Answers to Specific Consultation Questions	5
Q1	Do you agree with our assessment on the need for this supplementary guidance?	5
Q2	Do you agree with the purpose, scope and objectives for our proposed guidance,	5
Q3	Do you agree with our assessment of the options and our provisional conclusion in favour of a wholesale-minus approach?	5
Q4	Do you agree with our considerations in terms of whose cost should be used in a wholesale-minus approach? Should the incumbent water company’s costs or cost of a reasonably efficient bench mark be used?	5
Q5	Do you agree with our proposed overall approach for setting bulk charges?	6
Q6	Do you agree with our proposed relevant starting point?	6
Q7	Do you agree with our definition and approach to estimate the ongoing on-site costs?	6
Q8	Do you agree with our discussion about the WACC? In particular do you think we should adjust the incumbent water company’s WACC as per the Priors Hall determination?	6
Q9	Do you have any practical suggestions on how to estimate the appropriate WACC?	6
Q10	Are there any other costs that we should take into account?	7
Q11	Do you consider that the proposed approach is sufficiently flexible to cover all current circumstances and could adapt to possible future changes?	7
Q12	Do you consider that it would be possible to standardise charges under many if not most circumstances?	7
Q13	Do you agree with our proposal for the provision of tariff information?	7

1. Introduction

This document provides South East Water's response to the consultation on bulk charges for NAVs issued in November 2017.

2. Answers to Specific Consultation Questions

Q1 Do you agree with our assessment on the need for this supplementary guidance?

Yes we do.

Over the last 10 years South East Water has seen very little NAV activity and has no NAV sites, however in the last 12 months we have seen numbers of NAV enquiries based on the unserved criterion and expect most of these will become NAV sites. This increased activity shows there is a developing, active market and additional clarity will benefit all parties and help participants deal with applications more efficiently.

Q2 Do you agree with the purpose, scope and objectives for our proposed guidance,

We agree with the purpose, scope and objectives of the proposed guidance as outlined in the consultation document.

Q3 Do you agree with our assessment of the options and our provisional conclusion in favour of a wholesale-minus approach?

We agree that wholesale-minus is a better approach to setting bulk charges for NAV sites than cost-plus. We agree that the cost-plus bulk supply price would be more complex to produce, with increased risk of errors and therefore more open to challenge and dispute.

Q4 Do you agree with our considerations in terms of whose cost should be used in a wholesale-minus approach? Should the incumbent water company's costs or cost of a reasonably efficient bench mark be used?

One of the objectives of competition is to encourage all parties to be more efficient and innovative leading to cost savings for developers and customers in the case of NAV's. Using a reasonably efficient bench mark will not provide the correct incentives and thereby could create inefficiencies in the market. Where you would expect least efficient incumbent water companies to be targeted as they offer the most incentives this would not be the case under the reasonably efficient bench mark approach.

Q5 Do you agree with our proposed overall approach for setting bulk charges?

We agree with the proposed wholesale-minus approach and this is in line with our current approach and process.

Q6 Do you agree with our proposed relevant starting point?

Yes we agree with the proposed relevant starting point and this is in line with our current approach to calculating NAV bulk supply prices. In particular we agree that the relevant starting point should be the set of incumbent water company's wholesale tariffs that reflects the NAV's potential end-customer base. However as circumstances could change over time we believe that the bulk supply contract should include a regular bulk supply price review process but limited to every 5 five years in line with the PR process. See Q11 for more detail on this.

Q7 Do you agree with our definition and approach to estimate the ongoing on-site costs?

We agree that the ongoing costs that need to be deducted from the relevant wholesale tariffs should reflect the activities that the incumbent would have performed on the NAV site and that the NAV is now expected to perform. We agree that we would use average maintenance costs that the incumbent can be expected to incur over the lifetime of the asset.

Q8 Do you agree with our discussion about the WACC? In particular do you think we should adjust the incumbent water company's WACC as per the Priors Hall determination?

We agree that the WACC for the on-site asset needs to be deducted along with the ongoing on-site costs from the relevant wholesale tariffs.

Q9 Do you have any practical suggestions on how to estimate the appropriate WACC?

No comment

Q10 Are there any other costs that we should take into account?

We believe the proposed wholesale minus approach to determining the bulk supply price for a NAV site already accounts for all the avoided costs.

Q11 Do you consider that the proposed approach is sufficiently flexible to cover all current circumstances and could adapt to possible future changes?

The bulk supply contract could provide an element of future proofing by requiring periodic reviews of the bulk supply price. To prevent this from becoming onerous reviews every 5 years seems reasonable and they should be line with each price review as this would allow the NAV bulk supply price review to take into account any outcomes from the PR which may impact on the NAV bulk supply pricing model.

Q12 Do you consider that it would be possible to standardise charges under many if not most circumstances?

The model and approach to calculating the bulk supply price but the charges themselves should not be standardised as site specific characteristics need to be included or market incentives could be distorted.

Q13 Do you agree with our proposal for the provision of tariff information?

We agree that bulk supply charging information as far as this is not site specific and including details of the incumbent water companies pricing model and assumptions should be published. This will allow for a more transparent market place and improve the efficiency of the process to create a NAV site.

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