

From: Davies Daniel D <DanielD.Davies@dwrcymru.com>
Sent: 08 January 2018 13:10
To: Charging
Cc: Davis Mike
Subject: Bulk charges for NAVs consultation

Re Bulk charges for NAVs: a consultation

Thank you for the opportunity to respond to this consultation. We note the guidance only addresses bulk supplies being requested by NAV's pursuing applications under the unserved criterion. We broadly agree with Ofwat's assessment of the NAV market and the need to issue supplementary guidance on charging for bulk services between incumbents and NAVs. However, we do believe that the final guidance will need to be supplemented with detailed mandatory charging rules that will provide further clarity and transparency, as noted below.

Our answers to the consultation questions are provided below.

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

Yes. Currently incumbent undertakers are required to interpret for themselves the requirements of the Water Industry Act 1991. As a consequence regional variations in charging policy have arisen as companies interpret the requirements differently.

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

We believe that in order to provide sufficiency clarity for both undertakers and NAVs Ofwat needs to go further and develop and publish detailed mandatory charging rules. This will avoid different interpretations that could lead to lengthy and costly disputes that are not in the interests of customers.

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

Yes. The wholesale minus approach would be simpler, but in order to work it would require detailed rules to be established. While a cost-plus approach would theoretically be a better option, in practice it would be difficult, time-consuming and costly to administer.

Q4 Do you agree with our considerations in terms of whose costs should be used in a wholesale-minus approach? Do you have a preference? If so, please specify the reasons for your preference?

Yes, we agree with the analysis in the consultation. Our preference is for efficient benchmark costs published by Ofwat to form the basis of the deduction from wholesale costs. We agree that using incumbent companies' costs may not lead to optimal outcomes in some situations. This would also have the advantage of making disputes less likely between undertakers and NAVs as to the calculation of the costs to be deducted.

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

We are content with the proposal provided it is supported by detailed prescriptive rules.

Q6 Do you agree with our proposed relevant starting point?

No we do not agree. While an “overall weighted average” is a reasonable proposal it would be prohibitively difficult to implement in practice, for two main reasons. Firstly, there would likely be limited knowledge of the make-up of on-site customers at the time of initial discussions with NAVs. Secondly, incumbents would have limited information on how the mix of on-site customers changed following the appointment of the NAV.

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

Wholesale tariffs reflect the regional average efficient short-run maintenance costs allowed in the price review. If the relevant wholesale tariff is the starting point, then it is logical that the ongoing on-site costs deducted should be the efficient costs allowed in the price review.

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 this is a complex area that requires further discussion and engagement. We don’t necessarily agree with the presumption that the difference in status between companies justifies a different WACC. If Ofwat were to try to set a ‘bespoke’ WACC for this purpose, it would raise all sorts of practical issues over the estimation of the appropriate WACC. We think the simplest approach, using the WACC determined by Ofwat at price reviews, may be the best.

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

We would welcome the opportunity to contribute to further debate on this issue.

Q10 Are there other costs that we should take into account? If so, please specify what these costs are and why they should be considered?

We would note that the recommendations within the consultation for the treatment of income offset are based on policy decisions made as part of the **“New connection charges for the future - England”** which do not apply in Wales. We would welcome clarity as to how Ofwat believe income offset should be treated in Wales. (We note that Section 144ZD of the Water Industry Act 1991 requires the Welsh Ministers to publish guidance which may be relevant to this issue.)

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

See comments above on our reservations concerning the proposed approach.

Q12 Do you consider that it would be possible to standardise charges under many if not most circumstances? Can you specify the circumstances where this may not be possible?

It should be feasible to publish the tariff formulae and the pricing inputs that the undertakers would apply. NAVs could use these formulae with their own site specific inputs (e.g. forecast end customers) to estimate the expected bulk supply charges.

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

Yes we agree, subject to the comments made above.

Yours sincerely,

Daniel Davies
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Dwr Cymru Welsh Water

Dwr Cymru Welsh

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