7 September 2020

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BY EMAIL TO: NAVpolicy@ofwat.gov.uk

Ofwat
Centre City Tower
7 Hill Street
Birmingham
B5 4UA

Dear Ofwat,

Portsmouth Water – Response to Ofwat Consultation on bulk charges for New Appointments and Variations (NAVs)

Thank you for the opportunity to review and comment upon the above consultation published in July 2020.

We welcome this consultation and the review by CEPA and agree that it is important that there is a well-functioning NAV market to allow increased choice, efficiency and innovation.

We have responded to all 12 questions in the Consultation as attached.

If you have any questions on the detail in our response, please contact me.

Yours faithfully,

[redacted]

HELEN ORTON
Finance and Regulation Director

Ofwat Consultation on Bulk Charges for NAVs

Q1: Do you agree with our proposed approach to weighted average tariffs?

We agree with the Ofwat position that the weighted average tariff should be site specific taking into account the actual mix of end consumers and their consumption rather than relying on a typical mix of end consumers.

Q2: Do you agree that large user tariffs should not be offered for new NAV sites? What should the approach be to existing sites?

We agree with Ofwat that large user tariffs should not be offered for new NAV sites. We suggest that for existing sites the NAV tariff should apply as of the start of the 2020/21 charging year.

Q3: Do you agree that incumbents should use bottom-up approaches to estimate costs, or would more granular accounting segmentation be more appropriate?

We are comfortable using the bottom up approach to estimate costs. We have based ours on our Accounting Separation Methodology and feel that this is an appropriate level to use. It also has the benefit of being transparent and aligned to the wider regulatory framework.

More granular accounting segmentation would be time consuming to establish – though would result in a more precise value of the costs avoided.

Q4: Do you agree with CEPA's list of common avoided costs or should additional items be included? Should we incorporate this list in our guidance?

The list provided in Appendix B of the CEPA report is helpful. We cannot think of other costs to be included.

We would welcome this being included in the Ofwat guidance.

Q5: Do you agree with our proposed treatment of indirect costs?

We agree that the inclusion of indirect costs in the avoid cost calculation will result in greater "discounts" to NAVs and may encourage greater entry.

We are not sure what Ofwat mean by common costs and would welcome clarity on this issue. That said, we note that Ofwat are clear that we should only subtract avoided costs, which, in reality will not include indirect costs which in turn will result in lower discounts to NAV sites.

Q6: Do you agree with our proposed approach to capital maintenance and replacement expenditure?

We note and agree with the use of a bottom up approach to capital maintenance and replacement expenditure. We agree an average annuity approach would overcome the issue of timing etc.

Q7: Do you agree with our proposed approach to the income offset for Welsh incumbents?

We note the different approach to income offsets in Wales. We suggest Ofwat should continue to be prescriptive on the rate of return to apply to the onsite assets, to ensure consistency with general prices for the two operators in Wales.

Q8: Do you have other comments on the rate of return with respect to English incumbents?

None. We note there will no longer be a rate of return deduction in the NAV tariff.

Q9: Should our guidance explicitly state that bulk charges should not financially penalise NAVs for promoting greater water efficiency?

We note and acknowledge the lack of incentive to promote water efficient homes by NAVs and agree a requirement that NAVs should not be worse off should be explicit in Ofwat guidance.

Under our scheme the NAV would be neutral in terms of the on-going NAV tariff whether it installs water efficiency or not, as we would base the weighted average tariff on the assumed volume.

Q10: Do you agree with the principle that NAVs should have discounted charges if they deliver sustained lower per capita consumption (and similarly improved outcomes with respect to rainwater volumes and sustainable drainage) based on avoided costs or environmental impact mitigated?

We also agree that (in principle) the NAV delivering sustained lower PCC should receive a greater discount on its charge.

Q11: Do you have other comments you wish to make regarding the methodological issues set out in CEPA's report?

We were pleased with the assessment CEPA made of our NAV tariff. We are company A in the CEPA report.

We note the variation in "discounts" being given by each company and agree it is likely to be methodological issues as opposed to fundamental cost differences.

Therefore we suggest that Ofwat should be more prescriptive rather than less prescriptive in any guidance it publishes.

Q12: What are your views on how changes to bulk charges for NAVs might best be implemented?

Each of the 4 approaches have merit

1. We will review and update our methodology for 2021/22 in light of the CEPA report.

2. We note the success of the industry led group and would support this approach if adopted. Clearly this approach will use 1 above as a significant input to any of its conclusions.

3. We believe the most effective approach to ensure consistency between companies is the prescriptive nature of any Ofwat guidance. This approach could use 2 as an input, ensuring industry knowledge is applied and by default industry agreement and buy-in is achieved.

4. We would support this option overall, notwithstanding the concern that there may be issues with particular sites which are atypical.

We will revise our 2021/22 NAV charges as a result of this consultation.