

Our Ref: PK/LAT/Ofwat

Your Ref:

7 September 2020

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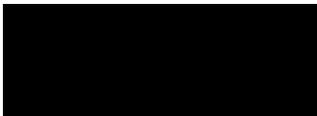
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Dear Ofwat,

Thank you for the opportunity to provide our views on the bulk supply charges consultation for the Newly Appointed and Variations (NAVs). While we do not have any NAVs operating in our area at present, we have provided responses to the majority of consultation questions and are happy to discuss further as needed.

We do not object to these responses being published on Ofwat's website.

Yours sincerely



Paul Kerr
Group Chief Financial Officer

Appendix. SES' Response

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

Response: We agree with the proposed menu-based approach when defining the relevant wholesale tariffs. SES Water's bulk supply charging arrangements for NAV's reflect a weighted average of the mix of residential and business properties on a NAV site, in line with the transparent menu-based approach proposed in this consultation.

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

Response: We agree that large tariffs should not be offered for new NAV sites. SES Water's charges for NAV's are calculated on a wholesale minus basis as per Ofwat's current guidance.

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

Response:

We support the use of top-down costing wherever there are sufficient commonalities across companies and sites to allow comparability and accountability of NAV charging across water companies. However, we do acknowledge that the use of a more granular accounting separation would help ensure cost-reflectivity for the last-mile infrastructure. While bottom up modelling approaches can in theory be more cost reflective, their use may not be transparent given that different companies can adopt different approaches and different levels of granularity. Bottom up models can also be resource intensive and costly to build and maintain which would disadvantage smaller water only companies – this is would be the case for SES Water as we currently do not have any NAV sites in its charging areas and therefore further development of an on-site asset management costing system would need to be considered.

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?

Response: We agree that the publication of a list of common avoided costs that Ofwat would expect to be excluded would help improve consistency and transparency in the calculation of NAV bulk supply charges.

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

Response: We agree that the calculation of the bulk charges for NAV's should take account of common cost avoided as a result of a NAV operating the site.

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

Response: We agree that capital maintenance costs for a NAV site should be excluded where relevant.

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

Response: N/A for SES Water

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

Response: We agree with CEPA's findings on the rate of return that with the changes to the income offset for English incumbents from 1 April 2020, where on-site assets are now funded by developers, the rate of return element will no longer apply. In addition, we agree that in terms of an additional allowance, to consider the operational risk experienced by NAVs to operate on-site assets which the incumbent has avoided.

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

Response: We believe that Ofwat should provide more specific guidance to address the perverse incentives for NAVs to increase water consumption. At the same time, there should be incentives for NAVs to invest and promote water efficiency without being financially penalised.

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?

Response: We agree with the above principles that NAVs should have discounted charges if they deliver sustained lower per capita consumption based on avoided costs or environmental impact mitigated.

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

Response: CEPA has made a number of useful observations and recommendations to improve transparency and compliance in the calculation of bulk charges for NAVs, which SES Water will consider in their review of future bulk charges for NAVs.

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

Response: CEPA has identified that there is a good level of basic compliance with Ofwat's guidance for bulk charges for NAVs. We therefore support their proposal that the bulk supply charging policy can be developed by an industry-led process overseen by Ofwat.