

From: 
To: 
Cc: 
Subject: Response to Ofwat Bioresources Review
Date: 22 July 2021 15:26:10
Attachments: [image001.gif](#)

Dear Connor

We welcome Ofwat's review of the bioresources market and the opportunity to respond. We fully support the efforts to explore the benefits of markets in bioresources services and are keen to support the development of an effective market in this area. We agree with many of the findings of the Jacobs report concerning the features of the current framework which are constraining the expansion of trading. We would like to draw attention to some of these, and we also comment on Ofwat's position on the design of the price control.

The document comes at an interesting and challenging time for the bioresources industry. At present wastewater companies are very concerned by the threat of restrictive legislation from the Environment Agency (proposed land management reforms) and Natural Resources Wales (an 'all Wales' Nitrate Vulnerable Zone). These changes are likely to place limitations on the disposal of treated sludge to land, by far the lowest cost disposal route. (The principal alternative to disposal to land is incineration, which is both higher cost and bad for the environment in terms of moving the industry towards a carbon neutral future.) Until there is greater clarity on this issue, including who is responsible for what under the new regulations, companies are unlikely to enter into serious discussions on long-term trades, and potential market participants will be reluctant to commit capital.

Like many companies, we are currently engaging in short-term trading as part of normal business practice, to deal with fluctuations in capacity around maintenance periods for example, and to assist in a pro-competitive way other companies similarly. However, there is very limited long-term trading of bioresources service on a more substantial basis. The review correctly identifies many of the challenges that would need to be overcome before long-term trading becomes more mainstream. These include the regulatory treatment of long-term trading costs, the contractual sharing of risk, pricing and competition rules, and the regulation of co-treated wastes.

Ofwat also correctly identifies a co-ordination and timing problem. Trading has the potential to play a more significant role when companies are investing in replacing their sludge treatment assets, as currently there is very limited excess capacity for trading. But such investment is 'lumpy' and infrequent. Companies may be investing in significant additional capacity in the medium-term in anticipation of higher nutrient removal requirements from the environmental regulators. If two neighbouring companies were considering an investment at the same time, the potential for trading, potentially with the involvement of a third party, would be there. The publication of the additional bioresources information will help to identify such opportunities.

In terms of the design of the price control, Ofwat is considering moving towards a benchmarked average revenue control. We note that this was also considered as one of the options for PR19, but was rejected exactly because of some of the difficulties and complexities identified here, including RCV protection and asset stranding. Benchmarking of sludge totex will also be problematic because of the 'lumpy' nature of capital investment in sludge capacity. We would propose that it may be beneficial for the bioresources working group to seek solutions to some of these challenges.

On some of the specific issues:

- On the bid assessment framework, we believe this is proportionate and would help ensure that third party bids for trading are not disadvantaged.
- We welcome the additional standardised guidance on the allocation of overheads, energy revenue, sludge liquors.
- We agree that a measure of sludge quality would be useful, though the issues are complex and there may not be a single measure that can helpfully capture sludge quality.

We are committed to working with the rest of the sector and other stakeholders to find solutions for these challenges, and ensure we maximise the potential benefits of market forces in this area.

Yours,

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