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PR24 Methodology - Ofwat Consultation
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07 September 2022

Dear Sir / Madam,

RE: Consultation on PR24 Methodology

Thank you for the opportunity to respond to this consultation. As you may be aware, ESP Water was appointed as a New Appointment and Variation (NAV) company in July 2022, and we therefore respond to this consultation in that capacity.

In general, we are supportive of Ofwat's ambitions and goals for PR24 and its continued commitment to an open and collaborative approach to determining price controls. We are also supportive of Ofwat's decision to continue to exclude NAVs from requirements of the price review (as we have Condition B in our appointment relating to the 'no worse off' principle) as this is a fair and proportionate approach. Of relevance to us as a NAV are Ofwat's proposals relating to developer services and consequently our comments relating to this topic are included below.

Firstly, your methodology includes a review of the developer services market since PR19, which is useful. However, we would disagree with your assumption relating to water site specific developer services work for sites with <25 plots not being delivered by SLPs as this number depends hugely on the bulk supply tariff offered by the incumbent water company we wish to take a supply from. Whilst smaller developments are particularly sensitive to this and often results in them being uneconomic and defaulting to the incumbent, this is not restricted to the <25 plot sites and, in some regions, can be a significantly higher threshold. In some cases, a site is not financially viable even for comparatively large sites. We would therefore suggest that Ofwat should place greater emphasis on regulating bulk supply and discharge tariffs and incentivise transparency and good performance, potentially taking an upper quartile approach, where competition is promoted. Otherwise, inefficient incumbents are rewarded with less competition from NAVs.

For the specific questions and comments in the consultation that we wish to respond to we have copied your questions in blue and our reply is in black.

Developer Services – Price Control

[Q3.2. Do you agree with our proposals to:](#)

a) Continue to include network reinforcement in the network plus price controls?

Yes, we agree with this proposal.

b) Remove wastewater site specific developer services from the wholesale wastewater network plus price control?

Yes, we agree with this proposal if the outcome does not hinder development or competition. We would be interested in the views from the incumbents on this question as some incumbents could improve their engagement in this area and taking it out of the price control could mean they need to be more effective.

Q3.3. Do you agree that the inclusion of network reinforcement in cost sharing would be enough to manage uncertainty around the volume and mix of network reinforcement work to be delivered?

“We are seeking stakeholders views on whether to apply a reconciliation mechanism to network reinforcement investment requirements similar to the DSRA at PR19”.

In answering these two points, we are supportive of network reinforcement staying within price controls but would support a mechanism over and above cost sharing to account for differences, like the Developer Services Revenue adjustment (DSRA) as you suggest but again, we would like to understand incumbent’s views on this as part of this consultation.

Q3.4. For water site specific developer services:

a) Do you agree with our proposal to exclude new developments of more than 25 properties from the wholesale water network plus price control at PR24, but with transitional arrangements for companies with low levels of competition?

No, see below.

b) Do you think that new developments of 25 properties and fewer should remain in the wholesale water network plus control or be removed? If they were removed from the price control, what alternative protections could we introduce

As we have stated earlier, we don’t believe this can be considered in isolation from the bulk tariff charges and therefore that the trigger of 25 is the right way of determining this threshold. We must see consistency between incumbents where their tariffs are cost reflective and transparent. We would recommend that this threshold could be something for the future, not PR24, once the issues surrounding the tariffs are resolved.

D-Mex

Q5.4. Do you agree with our proposed approach to the measures of experience performance commitments, including to increase the size of D MeX?

We are very supportive of the introduction of D-Mex in PR19 and believe it has improved performance amongst the incumbents. We understand that you would like to gather more data before making changes, however we recommend making any improvements that have been identified now rather than waiting.

Nutrient Neutrality

We propose to allow funding through the price review if water companies are required to go beyond environmental requirements due to nutrient neutrality in England. We expect developers to pay the full costs for any nutrient mitigation. We also plan to develop a reconciliation model for incumbents to correct for variances in actual vs expected NN developer contributions.

Q6.8. Do you agree with our proposed approach to implementing nutrient neutrality in the PR24 regulatory framework?

We disagree that it is always appropriate for developers to take on the full cost of any nutrient mitigation as this could seriously hinder development in certain areas. We would argue that in certain locations, incumbents should do more to improve nutrient reduction in their own wastewater networks first, otherwise there could be a case where an incumbent could defer improvements until a developer comes along who is obliged to put in schemes.

Income offsets, Environmental incentives, and Ofwat Innovation Fund

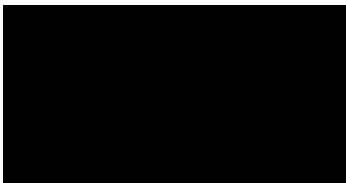
We understand your decision to avoid the introduction of transitional arrangements for the removal of the income offset mechanism but again would emphasise the need for incumbent tariffs to be consistent, transparent and cost reflective going forward.

With respect to environmental incentives, we are very supportive of Ofwat's proposals and believe, as a NAV, we are perfectly positioned to incentivise water efficiency and sustainable drainage (SuDS) schemes. We would however like to understand whether costs would be passed onto developers via NAVs should they wish to introduce such schemes? How would a NAV benefit for promoting such a scheme with a developer? Any introduction of an incentive scheme should ensure NAVs are not disadvantaged and that they are part of the process.

Finally, we are very supportive of the Ofwat Innovation Fund and would like to see it continue after 2025.

Should you require any further information on our comments, please do not hesitate to contact me.

Yours sincerely,

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ESP Water Managing Director