

New Appointments and Variations

The outcome of our consultation on 2019/20 bulk charges for NAVs

1. Introduction

The New Appointments and Variations (NAV) regime allows new entry into the wholesale water and sewerage sector. NAVs can choose to purchase a bulk supply of water and/or wastewater services from an incumbent. A bulk supply is the supply of water and/or sewerage from one appointed company to another.

In May 2018, Ofwat published final guidance on bulk supply charges for NAVs¹. The guidance suggests that incumbent wholesalers should adopt a ‘wholesale-minus’ approach to bulk supply charges for NAVs, which deducts costs avoided by the incumbent as a result of NAV activity from the relevant wholesale charge.

We conducted face-to-face meetings in summer and autumn 2018 to discuss our proposals with individual NAVs, which assisted in the further development of our proposed charges. Following this, we formally consulted on our proposed NAV bulk charges early in 2019. This document sets out the responses received and our corresponding decisions.

2. Changes to our Approach

While the responses contained some useful insight and helpful suggestions, we did not consider there to be any reasonable grounds or justification to change our methodology. Therefore, the methodology underpinning our final 2019/20 bulk supply charges for NAVs will be unchanged from those set out in our initial consultation.

¹ <https://www.ofwat.gov.uk/wp-content/uploads/2018/05/Bulk-charges-for-NAV-final-guidance.pdf>

The outcome of our consultation on 2019/20 bulk supply charges for NAVs

3. Consultation Responses

This section sets out the responses received and our corresponding decision. We provide additional explanation where necessary in the appendix.

Question	Responses	Uuw decision
<p>1 - Do you agree with our proposal to use standardised, rather than bespoke, NAV tariffs?</p>	<p>All responses agreed with our proposal to use standardised tariffs. For example, one response highlighted that a standardised approach provides more certainty for planning.</p> <p>One response noted that while the standardised approach is preferred, the charges should remain cost reflective.</p> <p>In addition, it was noted that the draft NAV bulk supply charge calculator still needs interaction with the incumbent before tariffs are finalised.</p>	<p>We will maintain our proposed standardised tariffs structure.</p> <p>Cost reflectivity is already required by Ofwat's charging guidance in respect of bulk supplies to NAV.</p> <p>The draft charge calculator was based on indicative charges. Now that final charges have been published, the tool will calculate final charges. Interactions with the company during the applications process were outside the scope of the consultation.</p>
<p>2 - Do you think we have identified all areas of avoided activity that should be reflected in the NAV discount? If not, then please explain what other areas of avoided activity we should consider.</p>	<p>Responses were generally supportive. One response confirmed that we had included all relevant avoided activities.</p> <p>One response felt that we had not provided sufficient clarity on the avoided activities, and provided its own list of activities.</p>	<p>We have retained our proposed view of avoided activity.</p> <p>We have explained our approach to each item on this list in appendix 1 below.</p>
<p>3 - Do you agree with our approach to compensating capital related costs via the income offset?</p>	<p>There were no objections to our proposed approach. One response stated that the income offset is a major contributor to making NAVs a more attractive proposition to developers.</p>	<p>We have retained our proposed approach.</p>
<p>4 - Do you agree with our proposal to offer a working capital allowance?</p>	<p>This proposal was supported. One response noted that it was not expecting a working capital allowance to be included, but that it would be beneficial.</p>	<p>We have retained our proposed approach.</p>

The outcome of our consultation on 2019/20 bulk supply charges for NAVs

<p>5 - Do you have any comments on our approach to reconciliation of outturn customer numbers, the bulk supply meter or providing an additional discount to sites where a customer holds a trade effluent consent with the NAV?</p>	<p>There were no objections to our proposed approach. One respondent did not agree that a NAV should fund the costs of the bulk supply meter.</p>	<p>We can confirm that we do not require NAVs to pay for the installation of the bulk supply meter. NAVs will only pay an annual meter standing charge in respect of that meter, which reflects future maintenance and replacement requirements. This is in line with our other bulk supplies' charging arrangements.</p>
<p>6 - Have we presented the tariffs in an accessible and transparent way or could this be improved?</p>	<p>One response requested more clarity and certainty on costs.</p> <p>Another response sought additional wording to demonstrate how the NAV charge will be applied</p> <p>Another response did not think there was a purpose in showing the discount per household.</p>	<p>We consider our final NAV bulk supply tariff will provide the desired certainty on cost. We trust that the additional information in appendix 1 and 2 provides the additional clarity.</p> <p>We have added additional wording into our final NAV bulk supply charges scheme, along with a worked example. We would also encourage NAVs to make use of the online NAV bulk supply charge calculator.</p> <p>We included the discount per household to provide a sense of scale of the discount. We have removed this from the final published charges scheme.</p>
<p>7 - Do you have any comments on our approach to surface water and highways drainage services?</p>	<p>We did not receive any comments on this question.</p>	<p>We have retained our proposed approach.</p>
<p>8 - What, if any, additional services could NAVs wish to purchase from U UW?</p>	<p>One response noted that it has had previous discussions with U UW regarding the provision of water sampling and emergency provision, and registered its disappointment that no significant progress has been made.</p>	<p>We confirm that we already provide accredited water sampling services to NAVs.</p> <p>We don't currently offer an Emergency Response Service (ERS) to NAVs, although we are keeping this position under review. We note that other companies in the North West are able to provide such services.</p>

The outcome of our consultation on 2019/20 bulk supply charges for NAVs

<p>9 - Do you agree that the service levels for the additional services offering should be the same as those we provide on our own network?</p>	<p>There were no proposals for alternative services other than our own. One response stated that U UW should offer equivalent services in terms of cost and quality to those already provided on its network.</p> <p>Another response stated that additional services should be based on the prevailing commercial rate.</p>	<p>We will use these responses as the basis of any additional service offerings that we develop.</p>
<p>10 - Do you agree with our proposed payment terms?</p>	<p>Responses supported our proposed payment terms.</p>	<p>We have retained our proposed approach.</p>
<p>11 - Do you have any other comments on our NAV tariff proposals?</p>	<p>One respondent was keen for there to be a dialogue between U UW and NAVs, including a review of how efficient the new measures have been following implementation.</p>	<p>We are also keen that there is open and transparent dialogue between U UW and NAVs. We offer quarterly liaison meetings with all NAVs; we can discuss the effectiveness of the new measures at this forum. In addition, we offer active NAVs in our area an invitation to our annual Developer Day. You can also contact us using our NAV mailbox: NAVenquiries@uuplc.co.uk</p>

4. Next Steps

Our final NAV bulk charges for 2019/20 have been published alongside this document.

NAVs currently active in U UW's region have the option to move over to the new NAV bulk supply charges. If this option is taken, we will backdate the new charge from the date we published the charges (12/06/2019) to 1 April 2019.

The outcome of our consultation on 2019/20 bulk supply charges for NAVs

Appendix – Information and analysis supporting UUW’s decision

Appendix 1 – Avoided on-site activity

In the response to question 2, one respondent shared its views of on-site avoided costs and did not feel we had explained with enough clarity what we had included in our NAV bulk supply discount. Table 1 sets out the activities suggested by the NAV and how UUW has addressed each one within its NAV bulk supply tariff.

Table 1 - On-site avoided activities suggested by one respondent

Reference	On-site avoided activity	UUW response.
1	Network maintenance of all on-site equipment	We provide a 100% discount against on-site customer meters. In addition, we include infrastructure repair costs based on competitively tendered rates.
2	Emergency cover	We include UUW’s general and support costs in the discount.
3	IT systems	We include UUW’s general and support costs in the discount.
4	Bad debt allowances for network costs	The starting point is the relevant wholesale end-user charge. Therefore, no deduction relating to retail costs is necessary.
5	General management and health and safety	We include UUW’s general and support costs in the discount.
6	Corporate overheads	We include UUW’s general and support costs in the discount.
7	Finance and HR	We include UUW’s general and support costs in the discount.
8	Regulatory costs	We include UUW’s general and support costs in the discount.
9	Capital maintenance	We include a capital maintenance costs that are based on competitively tendered rates.
10	Normal profit	We have included normal profit in the discount, as discounts are based on UUW’s costs including an allocation of profit. For example, excluding metering costs also excludes the normal profit earned on those assets. Additionally, where the deducted cost is based on contracted rates, an uplift for profit is included as this is contained within the contracted rate.
11	Customer support	The starting point is the relevant wholesale end-user charge. Therefore, no deduction relating to retail costs is necessary.
12	Water sampling and water quality	We have included a deduction for water sampling and water quality tests. This

The outcome of our consultation on 2019/20 bulk supply charges for NAVs

		deduction is based on UUW's commercial rate rather than the internal cost of providing this service.
13	Leakage (including site development)	<p>We include an adjustment that reflects on-site water losses. In addition to leakage, we reflect losses due to:</p> <ul style="list-style-type: none"> • Mains flushing • Mains rehabilitation • Use for construction purposes • Illegal use • Standpipe use

Appendix 2 – Reconciliation of a top-down and bottom-up approach

One of the respondents was concerned that we had not reconciled our wholesale minus approach with a bottom up approach. A bottom up cost plus approach is analogous to the old methodology, which was based on UUW's large user tariffs. This is because UUW's large user tariffs assume that large users do not use the entire distribution network, while recovering all costs incurred to the point of connection.

As Table 2 demonstrates, NAVs are better off under our new methodology for NAV bulk supply charges. This is the case across a mix of different sites.

Table 2 - reconciliation between a top-down and bottom-up approach

	Pricebase	Unit	Scenario 1	Scenario 2	Scenario 3	Scenario 4
Inputs						
Households connected on-site		nr	100	1,000	500	-
Non-households connected on-site		nr	5	-	10	150
Select 50 customers connected on-site		nr	-	-	1	2
NAV bulk supply charge - 2019/20	2019/20	£/m3	1.550	1.554	1.437	1.396
Select 50 fixed charge - 2019/20	2019/20	£/annum	19,550	19,550	19,550	19,550
Select 50 volumetric charge - 2019/20	2019/20	£/m3	1.401	1.401	1.401	1.401
Select 180 fixed charge - 2019/20	2019/20	£/annum	63,470	63,470	63,470	63,470
Select 180 volumetric charge - 2019/20	2019/20	£/m3	1.157	1.157	1.157	1.157
Total site consumption		m3	15,000	90,000	200,000	190,000
NAV charge calculations						
Total bill - new methodology	2019/20	£	23,250	139,860	287,400	265,240
Total bill - old methodology	2019/20	£	40,565	145,640	294,870	283,300
Difference	2019/20	£	17,315	5,780	7,470	18,060