



To: The Competition and Markets Authority

By email Only: Waterdetermination2020@cma.gov.uk

Ofwat Price Determinations
Competition and Markets Authority
The Cabot
25 Cabot Square
London E14 4QZ

25 June, 2020

Dear Sir/Madam,

Third Party Submission

In response to the CMAs recently published document¹ setting out its approach to the PR19 redetermination process, I am submitting this letter as Chairman of Waterlevel Limited, an independent and innovative investor in the water sector, the owner of the regulated NAV² Albion Eco Limited and a shareholder in the regulated NAV Albion Water Limited.

The following submission will focus on the water industry's delivery of growth infrastructure, in particular identifying how the regulatory regime fails to incentivise resilient, sustainable water service solutions to new communities and the perverse incentives that can drive sub-optimal solutions.

The opportunity for market-based solutions to meet housing growth requires a level playing field to be established and is wholly consistent with the development of Drainage and Wastewater Management Plans, soon to become a statutory requirement for Water and Sewerage Companies and specifically focussed on promoting partnership benefits.

It is suggested that neither the regulator nor the regional incumbents have established an efficient mechanism to determine whether local, community-based treatment facilities offer a better water services solution compared to capacity enhancement in, or connections to, existing network and treatment facilities when meeting the challenges of growth. In the absence of such a mechanism evidence is provided that, in many instances, sub-optimal solutions are delivered at higher cost, with greater carbon intensity, increased flow and quality risks to the water environment and missed opportunities to enhance biodiversity and the circular economy. It is plain to Waterlevel and, indeed, to many within the water industry that Ofwat's duties to promote effective competition, to secure long-term resilience, to promote sustainable development and to ensure the operation of fair markets do not receive adequate attention.

Waterlevel is grateful for the opportunity to contribute towards the current price redetermination and for the establishment of clear issues upon which the CMA wishes to opine. The following submission will seek to identify the main points as concisely and clearly as possible but there has been considerable additional background information generated during three decades dedicated to the benefits of introducing efficient competition in the Water Industry.

¹ PR19 Water redeterminations - Approach to the redeterminations.

https://assets.publishing.service.gov.uk/media/5ee21c85e90e070428c2c666/CMA_s_approach_to_water_redeterminations.pdf

² NAV – New Appointments and Variations are limited companies which provide a water and/or sewerage service to customers in an area which was previously provided by the incumbent monopoly provider.

Growth

Waterlevel supports the assessment methodologies employed by the water companies (based on local authority figures). It does not however support their current evaluation of options to deliver schemes to meet lowest costs whilst delivering higher levels of resilience and sustainability.

Two case studies highlight the scale of current inefficiency ‘baked into’ the existing regulatory regime.

	Case Study A South West England	Case Study B South Coast
Off-site requisition cost	£4.1m	£ low – local point of connection (by size, not capacity)
Infrastructure cost	NA	Approx. £30m
Treatment works cost	£6.8m	
Total water company cost	£10.9m	£30m
Price to the developer	£0.7m	£5m
Albion Water price for local community solution	£4.4m	£10m
Subsidy (payable by the generality of customers who have no choice of supplier)	Developer went with the incumbent offering (lowest price) benefiting from a £10+m cross subsidy from all regional customers	Developer chose a bulk discharge NAV together with the regional incumbent benefiting from a £20+m cross subsidy from all regional customers

In both of these cases the absence of optioneering in an open market, allowing access to the same cross subsidies that regional incumbents benefit from, results in:

- Greater cost to all regional customers (here totalling £15.6m assuming cross subsidies could have been diverted to the competitive alternative rather than the developer paying more)
- Higher operational carbon costs resulting from pumping effluent off-site
- Increased discharge and flooding from CSOs³
- Reduced flows in local watercourses

³ Combined Sewer Overflows, discharging untreated sewage to the environment during storm events, are a common feature of regional wastewater networks

- By-passing local aquatic wetland systems in favour of discharges downstream or out to sea
- Removal of local water recycling opportunities to reduce potable PCC⁴ <100 lpd
- Increasing the disconnect between community and impact on their local environment (flush and forget)
- Loss of opportunity to capture and reuse local nutrients, energy and water for irrigation

These outcomes could be categorised as ‘the scandal of downstream thinking’. Albion Water has been engaging with Ofwat over a number of years to remove barriers to NAV competition and has identified to them those aspects that present particular hurdles such as:

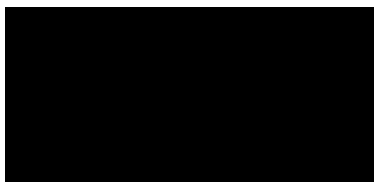
- Income offsets not being generally available for full-service⁵ NAVs
- New development connection costings based on size for size pipe connections even in the absence of available capacity
- Absence of a zonal infrastructure charge to differentiate the challenges of serving greenfield sites
- Provision of new wastewater treatment is free to developers (instead paid for by all regional customers through their bills)

In a sense the specific drivers for the case study outcomes are outside the remit of the current CMA redetermination; the important consideration is that greater efficiency is possible to deliver more resilient and sustainable growth at significantly lower cost. Were existing barriers to entry removed, full-service NAVs would be able to deliver better outcomes, without additional burden to developers, with lower costs to customers and with better totex outcomes for incumbents. This however is only likely to occur with effective regulatory intervention to removal those market barriers.

Waterlevel recognises that many large developments, particularly those close to existing networks and treatment plants with adequate capacity, will be best served by the regional incumbent – there is no one-size fits all. However, with the current barriers to efficient entry, NAVs have suffered the loss of numerous development projects, where the most efficient, resilient and sustainable solutions have been trumped by cross subsidy from dominant incumbents. We can provide further evidence on these cases should the CMA require.

In conclusion, Waterlevel submits that expenditure on growth infrastructure could be optimised by more efficient market utilisation and the fair and efficient allocation of any necessary cross subsidies - at a lower cost to end customers and, it is suggested, within existing PR19 determinations.

Yours faithfully



Dr Jerry Bryan
Chairman

⁴ Per Capita Consumption measured as litres per person per day (the current average PCC is around 140 lpd)

⁵ NAV operators can be broadly categorised as ‘bulk supply/bulk discharge’ or ‘full service’, only the latter investing in treatment and recycling infrastructure.