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Douglas Cooper
Competition and Markets Authority
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Dear Douglas

Ofwat's further submissions

Thank you for your letter of 23 June in relation to the further submissions made by Ofwat on 22 June. In that letter you asked if we could provide you today with a brief list of 'specific issues raised by the water companies that Ofwat consider are new and where these are specifically addressed' in the further submissions.

We sought to be very careful in our further submissions to confine ourselves to the three categories of submission referred to in our letter of 17 June and documented more fully in the Annex, together with a few corrections of company mischaracterisations also referred to in the letter. We understand, however, that you would find it helpful for us to identify the aspects of those submissions described in your letter.

To provide the most assistance to the CMA we have focused on the new issues and/or evidence that we consider the water companies have raised, and indicated where in our submissions we have responded to those issues and/or evidence with substantively new material.

Please find appended to this letter a table which seeks to identify the relevant parts of the submissions, as requested. In line with your letter, we have kept it as short as possible. We recognise that there is a need for some use of judgment in identifying what falls within your description. However, rather than attempt to document our thinking, we would be happy to explain anything that might remain unclear if you should ask us to do so.

We hope that this is helpful.

Yours sincerely



David Black
Chief Regulation Officer

Annex 1: Summary of Ofwat response to new points

Key Issue and description of new point	Where addressed
Anglian Water (see 'Response to Anglian Water's 27 May submission to CMA')	
Growth: Updated estimate of growth costs and new report by Vivid Economics. New Ofwat evidence relating to historical WRMP forecasts, in response to new analysis.	paragraphs 2.11 to 2.26
Capital maintenance: new evidence; including analysis of asset lives within the company's asset base and a new Oxera report. New arguments regarding our engagement with the company's evidence on operational resilience impacts and our 'future Asset Health project'.	paragraphs 2.27 to 2.45
Interconnector programme: our response to new company arguments about consistency of the scheme with National Framework and WRMP24 guidance.	paragraphs 2.54 to 2.55
PR19 framework: new document and arguments on impact of PR19 on incentive based regulation, in particular around the impact of reconciliation mechanisms.	paragraphs 4.3 to 4.4
Bristol Water (see 'Response to Bristol Water's 27 May submission to CMA')	
Company specific adjustment: new arguments on our updated small company premium estimate and additional evidence that its thin profit margins drive higher equity risk. New evidence on its cost of equity uplift testing with customers and annual bill impact for all uplifts. New Ofwat evidence to illustrate the company annual bill impact is too low.	paragraphs 2.4 to 2.20
Leakage: new arguments raised by Bristol Water that the leakage claim has been raised before and that substantive evidence was provided during the PR19 process.	paragraphs 3.5 to 3.8
Developer services & enhancement efficiency: new argument that there is an error in the calculation of the efficiency factor applied on the DSRA and in enhancement shallow dives.	paragraphs 3.10 to 3.11, 3.17 to 3.21
Northumbrian Water (see 'Response to Northumbrian Water's 27 May submission to CMA')	
Duties: we respond to the company's new argument about Better Regulation principles.	paragraph 1.12
Sewer flooding resilience scheme: we respond to new company arguments about its £82 million investment from base costs and new rainfall analysis.	Paragraphs 2.6 to 2.17
Other costs issues: our response to new company materials on frontier shift ; on real price effects , our response to analysis of the volatility of oil and electricity prices over time, and; on costs stretch , real unit operating expenditure and downside risk from adverse weather.	paragraphs 2.38 to 2.45.
Expected ODI RoRE: our response to new company analysis based on ten performance commitments.	paragraphs 3.2 to 3.3

Key Issue and description of new point	Where addressed
Leakage: we provide new evidence that the company's suggested approach is not practicable.	paragraphs 3.11 to 3.13
Yorkshire Water (see 'Response to Yorkshire Water's 27 May submission to CMA')	
Resilience impact of the final determination: new company report from Arup 'Strategic review of resilience'.	paragraphs 2.4 to 2.7; 2.9 to 2.11
Hull: new company report from Dieter Helm on long term and catchment approaches.	Paragraph 3.4
Phosphorus removal costs: our new evidence in response to new Oxera report and company evidence on base and enhancement costs.	paragraphs 3.8 to 3.11; 3.13 to 3.18
Common performance commitments: new company information on lack of robust comparative data for which we provide new analysis.	paragraphs 4.5 to 4.10
Asset health: new company evidence and Economic Insight report on asset health and incentive regulation	paragraphs 4.13 to 4.14; 4.21 to 4.25; 4.30 to 4.36
Performance commitments: new company evidence and argument on sewer flooding; water supply interruptions; mains repairs; and sewer collapses	paragraphs 4.42 to 4.50; 4.52 to 4.54; 4.58 to 4.59; 4.62 to 4.63;
Funding upper quartile performance: our response to new Economic Insight report on the additional cost of improved service.	paragraphs 5.4 to 5.20
Cross cutting issues (see 'Response to companies' 27 May submission to CMA – cross cutting issues')	
WINEP: New company argument that if a company has taken account of frontier shift then an additional adjustment does not need to be made to WINEP costs. New Ofwat evidence on significant outperformance of PR14 NEP business plan costs. Anglian and Yorkshire Water now clearly reject application of frontier shift to metering. New Ofwat evidence in response.	paragraphs 2.14 to 2.29
IED costs: New Northumbrian, Yorkshire Water and EA cost estimates. We provide new response on proposed uncertainty mechanism.	paragraphs 2.34 to 2.36
COVID-19: New company estimates of cost impacts. Ofwat new evidence on applicable reconciliation adjustments.	paragraphs 4.1 to 4.17
Risk and return cross cutting issues (see 'Risk and return - Response to companies' 27 May submissions to the CMA')	
Balance of risk and return: New argument from Bristol Water that cost sharing rates should be amended in response to bad debt exposure due to Covid-19. company arguments for different cost-sharing rates.	paragraph 2.13

Key Issue and description of new point	Where addressed
Allowed return – cost of equity: New AGRF consultancy report submitted by Anglian Water and Northumbrian Water on beta estimation. New company evidence challenging our approach on risk-free rate and use of market-to asset (MAR) ratios. We supply a Europe Economics report on beta as well as new analysis of residual MARs once non-equity factors are controlled for.	paragraphs 3.2 to 3.7 and 3.14 to 3.22
Allowed return – cost of debt: New Centrus report submitted by Yorkshire Water supporting its claim that its debt was efficiently incurred. New company arguments that our approach drives refinancing risk, exposes them to unmanageable risk of market movements, and that our use of recent bond issues to support our ‘outperformance wedge’ is unrepresentative. We supply new evidence on historical debt issued by disputing companies for non-operational reasons, and updated analysis of recent water bond issues.	paragraphs 3.25 to 3.43
Financeability: New company challenges to prior PwC argument that use of RCV run-off and PAYG does not adversely impact long-term financeability. New company evidence on financeability impacts of downside scenarios. We supply new evidence on changes to Moody’s assessment methodology since our determination, and responses to above issues raised by companies.	paragraphs 4.3 to 4.13 and 4.23 to 4.27 (and risk and return confidential annex)
Gearing sharing outperformance mechanism: New argument from Yorkshire Water that we changed our approach between ‘the Reference and the Reply’.	paragraph 5.3
Actual structures: We provide additional detail in response to Anglian Water’s claim we had not responded to its claims about the benefit of securitised structures and Yorkshire Water’s claims about its actual structure.	paragraphs 5.16 to 5.23
Europe Economics ‘Response to some key points on real price effects and frontier shift’	
<p>New responses/evidence in response to new company arguments/evidence including new Oxera report:</p> <ul style="list-style-type: none"> • proportion of spend on construction and its weight as a comparator sector • embodied technological change makes no difference to frontier shift efficiency • link between oil prices and energy prices and recent evidence on chemical costs. 	<p>p6-7 and p10</p> <p>p12-15</p> <p>p17-20</p>