

By email to: [REDACTED]
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Kip Meek
Inquiry Chair – Water Redeterminations
The Cabot
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17 December 2020

Dear Kip,

Post-hearing follow up

Thank you again for the Panel's time on 2 December to further explore our responses to your provisional findings and those from other parties.

I write having now reviewed the transcripts and materials from the main party hearings. This response, comprising this letter, the table of commentary on the Ofwat transcripts (annex 1), and the attached submission (annex 2), follows up on all the action points as agreed at our recent hearing. There is one exception, which is that we consider it better to provide the reconciliation to the 4.97% cost of embedded debt in response to the forthcoming consultation. The response also addresses material issues raised during other parties' hearings. Consistent with our previous approaches, we have adopted a "high bar" for responses, responding only on material or new issues.

We also note our further submission made to the CMA on 23 November which did not form part of the discussion at our hearing, but which the CMA has confirmed will be reviewed and factored into the CMA's considerations in reaching final views ahead of publication of the final redeterminations. This is particularly relevant to the shortcomings of Ofwat's analysis on embedded debt, which were repeated at the recent Ofwat hearings, and which I raised both in my cover letter and in the detail of our 23 November submission.

More broadly, for several issues raised in Ofwat's hearings, the position put forward by Ofwat is misleading and/or partial. This is despite the fact that we have previously provided evidence to the CMA and Ofwat on these issues. For example:

- **Dividend position.** We provided to the CMA on 12 August 2020 (following Ofwat's first hearing on 15 July 2020) details of the securitised structure and intercompany interest payments that do not constitute cash paid outside the regulated entity.



The underlying dividends paid to shareholders reflect a much lower amount than the position presented by Ofwat. Ofwat continues to misrepresent Anglian's position, including in its recent Financial Monitoring Report, published on 2nd December 2020. This report suggests that Anglian Water has paid a dividend yield of over 13% and notes this as the 'highest in the sector'. This is incorrect and misleading.

- **Embedded debt.** Ofwat has pointed the CMA to data in the APRs¹ to support its estimate of 4.44% against Anglian's estimate of 4.97%. As we explained in our hearing² the APR includes a short-term facility that Anglian drew down in March 2020 to deal with Covid-19. While required to be disclosed in the APR, it is short-term debt that has been incorrectly included in embedded debt calculations. This is but one of a number of factors explaining the difference, albeit the largest single factor. Furthermore, Ofwat is now suggesting considering floating rate debt. Our view is that it would not be appropriate to assume floating rate debt ex post for the notional company as this would penalise companies which have already issued fixed rate debt in line with benchmark allowances.
- **Alleged link between gearing and operational performance.** At the recent hearing Ofwat asserts that there is a detrimental link between higher gearing and operational performance to customers. Contrary to Ofwat's claim, we have provided detailed evidence in previous submissions to demonstrate that, for Anglian, securitisation has led to enhanced performance, as the management team is required to focus on the core business. Ofwat acknowledged this in its July hearing, stating "*Anglian appear to be very much the exception*"³. Anglian set out further evidence of this in its SOC, figure 99 page 331.

Implementation of the Redetermination

We and other appellants have shown the negative impact on customers should the implementation of the Redeterminations be spread across three years rather than four. Our recent discussions with CC Water and retailers suggest they would support an approach which allows earlier implementation if possible. We were also heartened by Ofwat's acknowledgement at its hearing that reflecting Redeterminations in 2021-22 charges was possible and that they are willing to work with the CMA to facilitate this⁴.

We accept that the CMA must ensure it has time to complete its Redeterminations robustly. However, we would like to have the option of implementing the Redetermination into our 2021/22 charges if possible. To preserve this option, the CMA would need to include both three and four years of K in its Redetermination. This will preserve our ability to spread the charges over four years to the extent that we can make the logistics work. We would be grateful if the CMA could indicate to the main parties whether it is able to do this as soon as possible, so we can reflect this in our charging and consultation processes.

¹ Ofwat first hearing (30 November 2020) transcript, page 33.

² Anglian hearing 2 December 2020, page 83, line 1.

³ Ofwat second July hearing (22 July 2020) transcript, page 28, line 22.

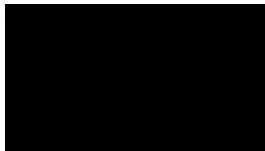
⁴ Ofwat second hearing (2 December 2020) transcript, page 94, line 25 and 26.

Early clarity on the scope of the Elsham DPC scheme

Following our hearing, we shared Mike Woolgar of WSP's independent review of Elsham DPC scope with both the CMA and Ofwat⁵. His review concluded that DPC should apply to the Treatment works only. Further to the conversation held with the CMA following the hearing, we recognise the CMA may wish to consult with Ofwat on this matter but would urge that it sets out a provisional view on the scope of DPC as soon as possible given the timing of successful delivery of the Elsham scheme is critical to ensuring the security of supply during AMP7.

Thank you once again for all the hard work that the Panel and the CMA team continue to put into the Redetermination.

Yours sincerely



Peter Simpson
Chief Executive

⁵ Letter dated 4 December 2020 from Anglian Water to CMA and Ofwat.