

**BEFORE THE COMPETITION AND MARKETS AUTHORITY**

**IN THE MATTER OF AN APPEAL**

**UNDER SECTION 23B OF THE GAS ACT 1986**

**B E T W E E N : -**

**WALES & WEST UTILITIES LIMITED**

**Appellant**

**and**

**THE GAS AND ELECTRICITY MARKETS AUTHORITY**

**Respondent**

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**SUPPLEMENTAL SUBMISSION  
TO THE  
NOTICE OF APPEAL**

**THE PR19 FINAL DETERMINATIONS**

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**Two Snowhill  
Birmingham  
B4 6WR**

**Tel: +44 (0)370 730 2878**

**Reference: 2663625/JAC/KXL3/RKR**

## 1 INTRODUCTION

- 1.1 Wales & West Utilities Ltd (**WWU**), together with other appellants, submitted its Notice of Appeal in these proceedings prior to the statutory deadline on 3 March 2021.
- 1.2 After the Notice of Appeal had been submitted, the CMA made its final report to Ofwat on the redetermination of the price controls of Anglian Water, Bristol Water, Northumbrian Water and Yorkshire Water (the **PR19 Final Determination**). The full text of this report was not published until 9 April 2021.
- 1.3 In its 'Note to parties on extension and revised timetable' dated 15 April 2021, the CMA stated that appellants should have an opportunity to '*make representations concerning the impact of the PR19 final determination on their NoAs*' by 23 April 2021.<sup>1</sup>
- 1.4 In providing this opportunity, the CMA made clear that –
  - (a) the purpose of any representations should be to clarify and update the case presented in the Notices of Appeal to take into account additional evidence introduced in the PR19 Final Determination, not to introduce new grounds of appeal or materially amend the reasons stated in the Notices of Appeal<sup>2</sup>, and
  - (b) it was expected that much of the updating would be to confirm or amend references to relevant aspects of the PR19 Final Determination in which the CMA had confirmed the position taken in its provisional findings or working papers<sup>3</sup>.

## 2 THIS SUBMISSION

- 2.1 WWU is grateful for the opportunity to make this short submission, which should be read with, and as a supplement to, its Notice of Appeal. It interprets this as an invitation to explain whether, and if so how, its Notice of Appeal would have been different if the PR19 Final Determination had been published before this appeal was commenced.
- 2.2 In line with the limits specified by the CMA, WWU therefore confines its representations to –
  - (a) the relevance of the PR19 Final Determination to the grounds that are already set out in the Notice of Appeal,

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<sup>1</sup> CMA – Note to parties on extension and revised timetable, para 16

<sup>2</sup> CMA – Note to parties on extension and revised timetable bid, para 13

<sup>3</sup> CMA – Note to parties on extension and revised timetable bid, para 14

- (b) the approach that WWU takes to the PR19 Final Determination for the purposes of the arguments which it makes in support of those grounds, and
- (c) the provision of some updated references to assist the CMA.

### 3 THE PR19 FINAL DETERMINATION

#### *WWU's Approach to its Appeal*

- 3.1 WWU's challenge to Ofgem's RIIO-GD2 licence modifications, as set out in its Notice of Appeal, was not materially dependent on the CMA's provisional findings in PR19, or any other element of the PR19 process. That position remains unchanged by the PR19 Final Determination.
- 3.2 The Notice of Appeal contained only three brief references to the PR19 provisional findings and/or consultation documents. At Annex 1 to this submission, WWU provides an update to those references – identifying where they have been reproduced in the PR19 Final Determination – in order to assist the CMA. But WWU does consider it necessary either to add to or expand upon them in the light of that Final Determination.
- 3.3 The PR19 Final Determination has no material bearing on the arguments advanced by WWU in support of its grounds of appeal. It may be useful to summarise briefly why this is the case.

#### *The Relevance of the PR19 Final Determination*

- 3.4 **First**, conclusions reached in previous CMA determinations may sometimes provide a useful guide, but they never constitute binding precedent. In determining every case that comes before it, the CMA makes what it considers to be the most appropriate decision in the particular context, having regard to all the specific circumstances of that case. It rarely, if ever, seeks to establish general rules of universal application.
- 3.5 Indeed the CMA expressed that position very clearly in its permission decision in this appeal, responding to Ofgem's representations that previous CMA decisions (including PR19) dictated a particular outcome to the treatment of WWU's cost of debt – *'the previous decisions of the CMA do not bind the group appointed to consider this appeal and do not in themselves demonstrate that WWU's Head A would have no reasonable prospect for success, given the specifics of this appeal'*<sup>4</sup>.
- 3.6 The CMA had also recognised the same point in the PR19 Final Determination itself – *'we are not bound by the decisions of other Groups in past redeterminations and appeals, where facts, issues and arguments are likely to have differed'*. It noted additionally that there is often limited

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<sup>4</sup> [CMA – WWU decision on permission to appeal](#) (31 March 2021), para 10

consistency in decisions made over time, due to changes in context or developments in policy – *‘in many cases the issues and approaches in these determinations have differed substantially from previous decisions’*.<sup>5</sup>

- 3.7 **Second**, the legal framework governing the PR19 redeterminations is fundamentally different from the one that applies to this appeal.
- 3.8 The PR19 redeterminations required the CMA to step into the shoes of Ofwat and make a fresh determination of the relevant price controls, as a *‘whole package...in the round’*<sup>6</sup>, following an examination of all the relevant evidence. The CMA was required to substitute its own judgment for that of Ofwat, applying the same statutory duties but using its discretion as an expert body to achieve what it considered to be the right balance of features across the price control as a whole. The process by which it did so lasted almost twelve months.
- 3.9 In contrast, the statutory framework under which the present proceedings are brought provides for a narrower and more focused dispute on limited heads of appeal identified by the appellants. The role of the CMA is to establish whether Ofgem made a decision that was ‘wrong’ on one or more statutory grounds. It must make that determination to a much tighter timescale than was available to it in PR19, and has a different range of remedies at its disposal. It acts in the role of appellate tribunal, not as a regulator remaking a decision in its entirety. Unlike PR19, this process is distinctively one of ‘appeal’, and not a redetermination.
- 3.10 **Third**, the legal framework, regulation, industry structure, and circumstances of the water and energy sectors are different in fundamental respects.
- 3.11 The companies involved in the PR19 redeterminations provide water and (with one exception) wastewater services directly to consumers. The water industry is responsible for the supply of water and removal of wastewater, as well as the infrastructure which allows those services to be provided. In contrast, in the gas distribution sector, companies do not carry out an end-to-end role leading to the supply of consumers, but are responsible for providing infrastructure, networks and services to shippers and suppliers. The historical development of the sector, and its current structure after disposals of companies at different times by National Grid, are quite distinct from the corresponding features of the water sector.
- 3.12 Moreover, the two industries are subject to different statutory frameworks, regulatory regimes and legal duties. In the water sector, there is a statutory duty on Ofwat to promote the resilience of future networks, which includes their readiness to meet the consequences of climate change (including increased flooding and water shortages). This is very different from the challenge

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<sup>5</sup> [CMA – PR19 Final Determination](#) (17 March 2021), para 3.20

<sup>6</sup> [CMA – PR19 Final Determination](#) (17 March 2021), para 110

applying in the gas distribution sector, as outlined to the CMA in the teach-in sessions, which is largely driven by the UK government's decision to legislate for Net Zero Carbon by 2050 and the implications for the investment climate of the technology and fuel uncertainty to which this gives rise.

- 3.13 Across a range of key features, the sectors are strictly non-comparable.
- 3.14 **Fourth**, the arguments before the CMA in this appeal are in many cases materially different to those that were advanced in the PR19 redeterminations, and therefore it is often difficult for any direct read across to be made.
- 3.15 For example, in respect of WWU's Cost of Debt ground (Head of Appeal A), we are not aware that any of the water companies in the PR19 redeterminations sought to develop its case before the CMA on the basis that the manner in which Ofwat had chosen to calculate the cost of debt was discriminatory. In that process, arguments relating to the nature and effect of the regulator's statutory duties were not predominantly reliant on legal (as opposed to policy) argument. The CMA was therefore not required to provide a ruling on these questions and, consequently, any decision reached on PR19 could not provide a template for this appeal.
- 3.16 By way of further example, on WWU's Cost of Equity ground (Head of Appeal B) Ofgem's proposal to make an ex ante outperformance adjustment to the cost of equity was not before the CMA, nor was the investment horizon or the impact of the Net Zero Carbon policy on the gas distribution networks considered. The CMA will be required to consider all of the arguments in respect of the Cost Equity *ab initio*.

*Ofgem's Position on PR19*

- 3.17 In spite of certain arguments that Ofgem sought to advance at permission stage in this appeal, it is on record as agreeing – indeed strongly advocating – that there are significant difficulties in attempting to read across from the PR19 redeterminations to the energy appeals.
- 3.18 In submissions to the CMA as a third party in the PR19 process, Ofgem was keen to emphasise the distinctions between the water and energy sectors, the different legal regimes under which the CMA acts in each sector, and the absence of any precedent effect created by the water redeterminations for the RIIO-2 price controls.
- 3.19 For instance, in the introduction to its submissions on the CMA's PR19 provisional findings, it said the following –

‘We also recognise that the CMA's statutory role in references in the water sector requires it to carry out a de novo assessment; the PFs provide as follows:

*When a reference is made to the CMA by Ofwat (on request of a water company) for a redetermination of Ofwat's price control, the CMA is to decide the matter on its own merits in accordance with the statutory duties that apply to Ofwat...*

*In carrying out these redeterminations, the CMA will be exercising its own regulatory discretion as to how to appropriately balance these statutory duties. As the CMA is making a fresh determination, the CMA considers that it should, in principle, consider any further issues that have arisen since Ofwat made the disputed determinations.*

We note that this is materially different to the CMA's role in energy licence modification appeals, which was described by the CMA in the RIIO-ED1 price control appeals as follows:

*We do not consider that an appeal under EA89 involves a rehearing where it is open to us to decide matters afresh untrammelled by GEMA's decision...*

*Nor do we consider that we were required in the present context to have conducted a re-run of GEMA's original decision-making process or to have held a de novo rehearing of all the evidence. The CMA must limit its consideration to the specific grounds of appeal set out in EA89, to the extent that such grounds are raised by the appellants...*

Notwithstanding those differences, we are concerned that certain findings made in this re-determination process, as currently expressed, may be relied upon by our stakeholders to attempt to influence or challenge the RIIO-2 regulatory process...

We are therefore keen to ensure that the CMA's findings in this price determination are not treated as making broader assessments beyond the present and specific context of PR19 in the water sector, particularly in circumstances where subsequent regulatory decisions could end up being the subject of consideration by the CMA in future.

We recognise, as no doubt the Panel does, that there are important differences between the water and the energy sectors. However, differences in outcome in the regulatory process may result not only from differences in the industries in question but also by reason of the fact that different regulatory judgments may be made in relation to similar issues. Whilst it is, of course, for this CMA Panel to frame the terms of its findings as it see fit, Ofgem considers it would be of assistance to all regulated industries (and their regulators) if it were able to emphasise clearly in its final decision that (a) the decisions and judgments in this case concern its particular statutory role in relation to water and focus only on the water industry; and that (b) the nature of the decisions and judgements it is making here pursuant to its particular statutory role are of the sort which other regulators might reasonably reach differently where these are a reasonable and logical reflection of the evidence and circumstances pertaining to those sectors.<sup>7</sup>

3.20 Further, in its concluding remarks in the same submission, Ofgem said –

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<sup>7</sup> Ofgem – Letter: Akshay Kaul to Kip Meek (29 October 2020), paras 2 to 7 (emphasis added)

'As set out in our introductory remarks, we also invite the CMA to make it clear that the findings in this price determination concern the CMA's particular statutory role in relation to water and focus only on the water industry, and should not be read across to other regulatory contexts. As the CMA will no doubt appreciate, different regulators can reasonably take different views on these issues.'<sup>8</sup>

- 3.21 As this makes plain, Ofgem argued strongly that there should be no read across from PR19 to the current energy appeals, requesting the CMA to make it clear that its findings concerned the particular statutory role in relation to water and could not be read across into other regulatory contexts.
- 3.22 Ofgem's submissions on this point are largely consistent with WWU's approach to the relevance of the PR19 Final Determinations, and for substantially the same reasons, as set out above. WWU agrees with Ofgem that these cases involve different considerations in different industries subject to different legal frameworks, and in which the role of the CMA itself is also considerably different.

#### *Conclusion*

- 3.23 The case advanced by WWU in its Notice of Appeal is premised on the specific circumstances of the company and the gas distribution sector as a whole, the legal framework within which it operates, the duties to which Ofgem is subject, and the requirements of sound regulatory policy in the light of all of these features.
- 3.24 The grounds of appeal invite the CMA to consider the case on its merits, in the light of these specific facts, laws and circumstances, and taking into account the evidence provided in support of WWU's submissions.
- 3.25 WWU was careful to provide detailed contextual information about the risk environment in which it operates<sup>9</sup>, to distinguish the water from the gas distribution sector<sup>10</sup>, and to emphasise clearly the extent to which its case is grounded in the specifics of its particular circumstances (and the particular decisions made by Ofgem) rather than in cross-sectoral generalities<sup>11</sup>.
- 3.26 For all of these reasons, the WWU appeal stands on its own pleaded terms, makes only passing references to PR19, and has no material dependency on the PR19 Final Determination.

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<sup>8</sup> [Ofgem – Letter: Akshay Kaul to Kip Meek](#) (29 October 2020), para 78 (emphasis added)

<sup>9</sup> For instance at Part I, Section 4 of the Notice of Appeal, outlining the current risks and uncertainty in the sector

<sup>10</sup> For instance at paragraphs B4.4 to B4.8 of the Notice of Appeal, on the asset beta

<sup>11</sup> For instance at paragraphs A3.4 and A3.5, in relation to the cost of debt

- 3.27 WWU invites the CMA to determine the case on the terms originally advanced, and does not believe that it needs to address the CMA further on any aspects of the PR19 Final Determination or seek to develop its Notice of Appeal by additional references to elements of that document. However, if the CMA should wish to be addressed on any elements of PR19, then WWU would of course be happy to do so in response to any questions that may be put to it.

#### **4 UPDATING REFERENCES**

- 4.1 In order to assist the CMA, WWU has identified, in the table at Annex 1, references to elements of the PR19 redeterminations that were included in the Notice of Appeal, and has provided the corresponding reference to the same statements in the Final Determination (where applicable).



**Annex 1 – References to PR19 in the Notice of Appeal**

Paragraph	Quote/Reference	Updated Reference
A6.8	<p><i>'The companies may reasonably expect that if issuing straight debt plus a swap instrument were economically equivalent but more flexible than issuing index-linked debt (at any particular moment) these two approaches should be treated equivalently in any assessment of actual costs.'</i></p> <p>Tab D34: CMA – Water Redeterminations – Cost of Debt – Working Paper, para 176</p>	<p>[Quote unchanged]</p> <p>[No corresponding reference in PR19 Final Determination]</p>
B6.10	<p><i>'Incentives are part of normal regulation and operational outperformance is a desirable outcome'</i></p> <p>Tab D34: CMA – Water Redeterminations 2020 – Cost of Debt – Working Papers, para 81</p>	<p>[Quote unchanged]</p> <p><a href="#">PR19 Final Determination</a>, para 9.1334(a) (page 1081)</p>
E9.3	<p>There is no way of quantifying the theoretical effect of the regulatory regime on x-inefficiency.</p> <p>Tab D33: Competition and Markets Authority – Anglian Water Services Limited, Bristol Water plc, Northumbrian Water Limited and Yorkshire Water Services Limited price determinations – Provisional findings, para 4.295</p>	<p>[Unchanged]</p> <p><a href="#">PR19 Final Determination</a>, para 4.493, fifth bullet point (page 232)</p>