

Significant changes in our wholesale charges

2020-21

Draft Wholesale Access Charging Rules, published by the Water Services Regulation Authority (WSRA), under sections 66E and 117I of the Water Industry Act 1991, require that if Severn Trent Water intends to make any significant changes to its wholesale access charges, it should provide to the WSRA and publish a statement of significant changes no later than the July immediately preceding the Charging Year for which the changes would have effect.

Below we set out changes we are making across 5 five areas:

- Fixed charges for unmetered customers
- Highway drainage charges (consistent with the Charging Rules);
- Non-household charges for water;
- Non-household charges for waste
- New appointments and variations

We also note that in 2020/21 our charges will be updated consistent with Ofwat's 2019 Final Determination, due to be published in December 2019. Although this determination does not require any structural changes, it is useful to note that it will lead to a material change in revenues between AMP6 and AMP7. Our official K factors¹ for all controls are zero next year, because wholesale controls have been split into two wholesale controls for each service. However, it is possible to calculate effective wholesale K factors of +7.7% for water and -4.5% for wastewater.

- The positive "K factor" for wholesale water relates almost wholly to the reversal of in-period regulatory penalties. Water charges for 2019-20 included Outcome Delivery Incentives (ODIs) of minus £42.1m and a revenue correction of -£6.7m. These are reversed in year 1 of next AMP
- Likewise, the negative "K factor" for wastewater is influenced by a reduction in the level of in-period incentives. Wastewater charges for 2019-20 included ODIs of +£36.6m and a revenue correction of +£4.0m

Fixed charges for unmetered customers

Most non-household customers in our area that are still charged by rateable value pay a small fixed charge for each service that they receive (fresh water, foul water and surface water). At present these relate primarily to market costs such as fees from MOSL². We intend to implement a gradual increase in these charges, in order to reduce the proportion of the overall bill that is linked to rateable value.

Most unmetered households in the Severn Trent area currently pay no fixed charge. We will introduce a fixed element for each service. The initial level of the charge will be small, to avoid incidence effects on low bill customers.

¹ Real change in wholesale revenues before inflation

² Market Operator Systems Limited

Customers in Severn Trent zones 9 and 10 (i.e. customers that were previously served by Dee Valley Water) already pay a higher fixed (standing) charge for wholesale water. There will be no significant change to the level of this charge in the near future.

Highway drainage

Ofwat wholesale charging rules (rule 20) require sewerage undertakers in wholly or mainly in England to have a separate wholesale charge for highway drainage from 1 April 2020. Customers in our area of appointment are already paying for this service, but the costs are included within the other charges that they pay. We will introduce a simple fixed charge to cover this service. Given that this is a new charging component, our intention is that this should initially be set at a low level to avoid incidence effects for smaller customers.

For unmetered wastewater customers, the initial increase in the fixed charges described above will cover this increase; metered non-households will also see a small increase in fixed charges for highway drainage (with a reduction in the proportion of overall bills paid through other charges). At a wholesale level, there should be no impact on metered households as there will be a corresponding reduction in the residual standing charge they already pay.

Non-household charges for water

We intend to phase out seasonal charging. The level of charge and discounts applied for larger customers should no change as a result of this measure. Having looked at the pattern of seasonal usage for large and intermediate users in our area, we will stagger this change to avoid sharp changes in bills. Next year we will narrow the differential between peak and off-peak charges.

We currently apply Intermediate and Large User Tariffs (IUT and LUT) to any sites within Severn Trent's original area where usage exceeds the relevant thresholds (currently 10,000 and 50,000 cubic metres of water respectively). If usage falls outside the estimate at the beginning of the year, there is a reconciliation at year end.

Next year, we intend to make the IUT and LUT available to customers in our area that were formerly served by Dee Valley (DVW). Since the metered water charges for these customers are lower than the standard rate in the rest of the Severn Trent region, they will need a higher level of usage to benefit from the IUT or LUT.

Accordingly, it will be for customers (with the advice of their retailers) to opt for the IUT or LUT. We will apply the same approach for all sites in the Severn Trent area. We will assume that all existing IUT and LUT customers remain on the tariff unless notified that they wish to change. Once selected, the rate will apply for the full charging year.

For non-households that were previously served by Dee Valley we will also apply the wholesale fixed charge; as described above, the wholesale element of this charge covers market costs.

Non-household charges for wastewater

We currently charge for wastewater using a falling block approach. In order to simplify our charges, we will move to the same method and bandings as we apply to water charges – that is:

- A discounted volumetric rate with an intermediate fixed charge; or

- A higher discount on the volumetric rate with a higher (large user) fixed charge.

This is a different way of achieving the same result, so we do not believe this will have significant incidence effects for customers. We will convert the discount arising on the falling block approach to provide the same effective rate.

Customers (with the advice of their retailers) will select an Intermediate or Large User Tariff (IUT or LUT) for a site. We will assume that all sites using more than the thresholds based on last year's consumption (10,000 cubic metres and 50,000 cubic metres) will elect for the IUT and LUT unless we are notified that customers do not wish to be charged at this rate.

This change will not affect any customer discharging less than 10,000 cubic metres of waste water.

New Appointments and Variations

The New Appointments and Variations (NAV) tariff will alter to reflect new Ofwat charging rules. The "income offset" relating to the cost of new on-site assets will no longer be reflected within the bulk water charge as it will in future be applied through a rebate against infrastructure charges. This means that the discount included in the NAV tariff will reduce in future.

We will not apply these changes retrospectively. The discount for NAV sites which have already commenced or which are due to start before 1 April 2020 will remain at the existing rate, because operators will not be able to recover any difference in cost from developers and the rebate against infrastructure charges will not be available to them.

Stakeholder engagement on tariff changes

Retailers operating in our area have a dedicated account manager, and we have already begun to discuss these changes with retailers through normal channels. We also have a team responsible for dealing with NAVs and will discuss the impact of the changes in the NAV tariff with current and potential operators.

This document deals with wholesale charges and is primarily aimed at retailers, but we'll also be discussing the impact of these changes with CCWater, the customer representative body. We have regular meetings with CCWater and are required to consult with them in advance of publishing our Scheme of Charges.