**Portsmouth Water**

**Bulk Supply Charges for NAVs – 2023/24**

**1. Background**

This document explains our NAV charge for the year 2023/24, which starts on 1 July 2023.

Under existing legislation, Ofwat may appoint a new water company to supply a site (for water supply) if it is currently unserved by the incumbent water company, the incumbent gives its consent, or the premise is a large user of water of at least 50 Ml per annum.

Most Newly Appointed Variation (NAV) sites have to date been unserved sites and relate to a mixture of residential and mixed use developments. A developer of any new site has one of three options to provide water infrastructure on its site:-

* to work with the incumbent water company,
* to work with a Self-Lay Provider or
* invite a NAV to build and continue to provide services to end user customers

This document provides an illustration of the detail underpinning any ongoing tariff we would apply to the NAV situation.

We have reviewed the guidance published by Ofwat in January 2021 and in the future will need to work with NAVs in our area to meet the regulatory expectations, to ensure the price we charge will result in “efficient” market entry. The tariffs for this year are set by building on the 2022/23 methodology. They now include central overhead costs, and a more detailed approach to determining the costs forgone in order to fully comply with the Ofwat guidance.

We consider that the proposed tariff is appropriate for 2023/24.

*To determine a site-specific NAV tariff (as required in the Ofwat guidance) we will need to understand the detail of the site to be served by the NAV including number, usage volumes and length of mains. NAVs are therefore encouraged to talk with the Company at its earliest convenience.*

Any party wishing to discuss this tariff further or discuss a specific site should contact the Company using the details below:-

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**2. Approach to tariff setting**

To determine a site-specific NAV tariff (as required in the Ofwat guidance) we will need to understand the detail of the site to be served by the NAV including number of properties, usage volumes and length of mains.

Ofwat use the ‘wholesale-minus’ approach to determine a tariff if there is any dispute between the incumbent and the NAV on the appropriate tariff for bulk water. We will apply this ‘wholesale minus’ approach to any new NAV who requests a bulk supply of water from Portsmouth Water. The following explains the steps in determining a bulk supply tariff for the NAV.

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| 1 | Relevant Wholesale Tariff | this is determined by the number and usage of the expected customers on the site. |
| 2 | Avoided on-site ongoing operating and maintenance costs | these costs are implicit in the current wholesale tariff and will not be incurred by Portsmouth Water as the NAV will operate and maintain the local distribution system.  |
| 3 | Avoided company central overhead costs | these costs are implicit in the current wholesale tariff and will not be incurred by Portsmouth Water as the NAV will manage the overheads of its own business. |
| 4 | Avoided WACC on on-site assets | these costs are implicit in the current wholesale tariff and will not be incurred by Portsmouth Water as the NAV will own the local distribution system. Further, Ofwat have been prescriptive on the relevant cost of capital. |
| Equals | Bulk Supply Tariff | The relevant NAV tariff is determined therefore by subtracting steps 2, 3 and 4 from step 1. |

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Following discussions with NAVs during 2020/21 we have developed our tariff structure further.

Historically we had derived a unit price for water delivered. We have now developed the structure so that the volume charge is our measured wholesale volume charge and introduced a negative charge to reflect the additional discount the NAV will receive relative to our standard customers.

This is described further below and is supported by a detailed spreadsheet deriving the NAV tariff for various scenarios. It also allows NAVs to enter their site-specific details to allow them to calculate an indicative charge.

**3. Detail to determine the tariff**

The proposed tariffs are purely illustrative, with further detail given in the attached appendix.

To determine a site-specific NAV tariff (as required in the Ofwat guidance dated January 2021) we need to understand the detail of the site to be served by the NAV including number of properties, usage volumes and length of mains.

We explain below the detail of how we will approach the quantification of the any NAV tariff. The 2021/22 outturn costs are inflated by the November 2022 CPIH to ensure consistency with current tariff setting methodology.

**Step 1 – The Relevant Wholesale Tariff** – we have already published our 2023/24 wholesale tariffs. In particular, we have household and non-household wholesale standing charges and volumetric charges, which are applied to illustrative numbers relating to the site.

In scenario A we assume a mixed site with 300 households and 20 non-households with 108 and 420 m3 per property per annum consumption respectively.

***We quantify the wholesale revenue is £40,020 or a unit rate of £0.981 / m3.***

**Step 2 – On-site ongoing** – as part of our annual Accounting Separation exercise we quantify the total operating and maintenance costsfor the local network for 2021/22 as £4,278k, inflated to 2023/24 prices. Given we have a local distribution network of 2,858km we establish an operating and maintenance cost per metre length of network to be £1.496.

For this example, we assume 7.5 metres main for each household and 10m for a non-household. We quantify the length of mains on the new site to be 2.5 km.

***We quantify the onsite operating and maintenance costs would be £3,741.***

**Step 3 – Overhead costs** – as part of our annual Accounting Separation exercise we quantify the central overhead costsfor the Company for 2021/22 as £3,901k, inflated to 2022/23 prices. Total property numbers for the Company total 125,483, so we establish an overhead cost per property to be £31.09.

***We quantify the overhead costs would be £9,948.***

**Step 4 – Return** – we have applied a Cost of Capital of 3.11% to the above ground assets which will be owned by the NAV. We have assumed this is only the meter and chamber. We have assumed a unit cost of £286 per meter, implying a return per meter of £8.89.

***We quantify the return on 320 meters to be £2,846.***

**Step 5 – NAV Unit Price** – we deduct the costs ‘foregone’ from the wholesale charge to determine the NAV tariff, as well as a deduction of 3.5% for leakage.

**The NAV charge is £23,485, or a unit rate of £0.555 / m3, a reduction of 43% on the standard wholesale tariff.**

**Step 6 – NAV tariff** – we will charge the NAV at our standard wholesale volume charge and make a daily reduction to the bill to ensure the correct unit price is paid.

**The NAV will be charged at 0.8536 / m3 and a daily reduction of £31.00.**

**4. Scenarios**

The table below shows how the percentage discount varies depending on the mix of properties on the site as suggested in the Ofwat publication.

Four scenarios are provided varying the mix of properties on the site. Scenario A is the one described thus far; Scenario B has no non-households, Scenario C has twice as many households and Scenario D is non-household only.

The discounts relative to the wholesale charge varies by scenario.



The table below shows the detail of our calculation.





