



# Statement of significant changes to primary wholesale charges

(Published October 2021)

## (a) Introduction

This statement of significant changes is an update to the statement we published in August 2021, and is made under Ofwat's wholesale charging rules (rule A4) <https://www.ofwat.gov.uk/regulated-companies/company-obligations/ofwat-regulating-the-industry-compliance-requirements-charging/>. It sets out potential significant changes to our primary wholesale charges for the 2022-23 charging year.

Our primary wholesale charges are set out in Section 3 of our Wholesale Statement of Principles and Charges document which can be found on our website (<https://www.southernwater.co.uk/wholesale-charges>). They are the charges that we make under sections 66E and 117I of the Water Industry Act 1991, to water and sewerage licensees with a retail authorisation or a restricted retail authorisation. The charges relate to the supply of water and sewerage services, both on an enduring or temporary basis, and including:

- (i) fixed and volumetric charges and allowances;
- (ii) any other charges set out in Section 3 of our Wholesale Statement of Principles and Charges document in relation to specific circumstances or events.

This updated statement of significant changes is published alongside our indicative primary wholesale charges for 2022-23, in accordance with Ofwat's wholesale charging rules (rule A3).

**Note that there remains a level of uncertainty associated with the forecasts of developer activity, property numbers and consumption which underpin these wholesale charges as a result of the impact of the Covid-19 pandemic. There is also potential for inflation to be higher than what has been assumed in these indicative charges. We will ensure that when final wholesale charges are set in January 2022, these reflect the latest available data. This may result in significant changes in wholesale charges compared to these indicative charges.**

## (b) Significant changes in charging policy from the previous year

### Removal of non-household fixed charges

In 2017-18, we introduced a new transitional fixed wholesale charge for non-household customers. This was intended to help smooth the transition to the opening of the non-household retail market and reduce the risk of bill increases for larger customers. When we introduced these fixed wholesale charges, we made clear that they were temporary and that they would be phased out over time.

We removed the fixed wholesale charge for our wastewater charges in 2020-21 and reverted to fully volumetric charges. We intend to phase out and remove our water fixed wholesale charges over the current five-year price control period, but are committed to doing so in a way that does not lead to significant bill changes for customers. For the 2022-23 charging year we are proposing to delay the further phasing out of the water fixed wholesale charges, due to forecast increases in water charges arising from other factors. We expect to continue the phasing out of these wholesale charges from 2023-24.

### New ammonia charge

We introduced a separate wholesale charge 2021-22 for ammonia within the Mogden formula in that is used to determine trade effluent charges. This has provided more clarity for businesses on the costs of treating their ammonia discharges, enabling them to respond to these price signals. This change means our wholesale charges partly reflect the amount of ammonia discharged into the sewerage system and translates into lower wholesale charges for customers with a low ammonia discharge, and higher wholesale charges for customers with a high ammonia discharge, making the wholesale charges more cost-reflective. We set out a shadow charge in 2020-21 and a low charge in 2021-22 to ensure our customers could prepare for the charge being introduced in the following charging year. We have engaged with our trade effluent customers and will continue to phase in the charge in order to limit the bill increases for customers next year.

## (c) Factors affecting the level of our charges for 2022-23

### Inflation and price limits

Our wholesale charges for 2022-23 will reflect the K factors set by Ofwat as part of the 2019 price review along with the impact of ODI penalties in year 1. They will also be uplifted for inflation, as measured by November 2021 CPIH, the latest forecast for which is 3.35%.

For our wholesale water charges, the combined impact of the K factors and ODI penalties for the water resources and water network + price controls is (3.4%). For our wholesale wastewater charges the impact of the K factor including ODI penalties for the wastewater network + price control is (7.5%). The price control for Bioresources is a total amount of revenue set as out in the Final Determination, modified to reflect the latest forecast sludge production for the charging year.

### Forecast consumption and connections

In setting wholesale charges we need to forecast the number of properties and consumption for the year ahead, to ensure that our charges recover our allowed revenues from the price control. The Covid-19 pandemic has led to significant changes in the water consumption of both households and businesses.

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Forecasting the ongoing impact of these changes will be very difficult. For the indicative wholesale charges we have forecast higher consumption from business customers as a result of a lower level of vacant properties and higher assumed consumption of the remaining customer base. This is offset by a forecast reduction in the level of household consumption. The forecast level of revenue from developers is also lower than that assumed by Ofwat in the final determination.

The aggregate impact of forecast demand on charges is to reduce bills.

**The level of wholesale charges is sensitive to changes in these assumptions. We will ensure that when final wholesale charges are set in January 2022, these reflect the latest data. This may result in significant changes in forecast wholesale charges compared to these indicative charges.**

### Impact of performance in financial year 2019-20 and 2020-21

Under Ofwat's regulatory rules, any under or over-recovery of revenues can be recovered in subsequent years. In 2020-21 we experienced a significant under-recovery of revenues, compared to the amount allowed under our price controls. This is recoverable in 2022-23. This results in a significant upward pressure on bills, in particular for wholesale water, where the impact is a greater than 10% increase.

In addition, the price controls set by Ofwat at the 2019 Final Determination reflected a forecast of the impact of our performance in 2019-20 (the so-called 'blind year'). Charges in 2022-23 will be based on our actual 2019-20 performance and not the forecast included within our Final Determination.

Ofwat has provided flexibility over the timing of adjustments associated with other aspects of our performance in the blind year. In aggregate, these would increase wholesale charges for both water and wastewater. We have decided to reflect only the blind year adjustments relating to wastewater revenue in our indicative wholesale charges as there is already significant upward pressure on water charges from other factors.

### Overall level of expected bill increases

The published wholesale indicative charges do not result in bill increases exceeding 5% for any group of customers. It should also be noted that, with the addition of retail charges, the average household water and waste bill increase will be lower than inflation.

These proposals are subject to review and approval by the Board of Southern Water Services Limited of the charges for final publication in our Wholesale Charges Schedule for 2022-23, required by 13 January 2022 ("Final Charges"). The level of Final Charges may vary from those of the Indicative Charges.