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IN THE COMPETITION
APPEAL TRIBUNAL

Case No. 1166/5/7/10

Victoria House,
Bloomsbury Place,
London WC1A 2EB

26 October 2012

Before:

VIVIEN ROSE
(Chairman)
TIM COHEN
BRIAN LANDERS

Sitting as a Tribunal in England and Wales

BETWEEN:

ALBION WATER LIMITED

Appellants

– v –

DWR CYMRU CYFYNGEDIG

Respondent

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HEARING (DAY 10)

Note: Excisions in this transcript marked “[...][C]” relate to passages excluded.

APPEARANCES

Mr Thomas Sharpe Q.C., Mr Matthew Cook and Mr Medhi Baiou (instructed by Shepherd Wedderburn LLP) appeared on behalf of the Claimant.

Mr Daniel Beard Q.C., Mr Meredith Pickford and Ms Ligia Osepciu (instructed by Hogan Lovells International LLP) appeared on behalf of the Defendant.

Friday, 26 October 2012

(10.30 am)

THE CHAIRMAN: Good morning. Good morning, Mr Edwards.

I gather there have been some developments.

MR BEARD: Yes. I don't know if the Tribunal wants to deal with those first of all?

MR SHARPE: I was rather hoping, madam, just to take you through a bit of housekeeping in relation to that document.

THE CHAIRMAN: Yes.

Housekeeping

MR SHARPE: We do have a short point to make on it. I think the Tribunal is familiar with the background, its origin and so forth.

THE CHAIRMAN: Not really.

MR SHARPE: Right. You will recall the cross-examination of Mr Edwards. Mr Edwards remarked that Welsh Water had engaged consultants in around 2000 to -- I think the words were "to look at the assets particular to all of the DC's non-potable networks".

THE CHAIRMAN: Is this connected with that document that we have seen a number of times? It's not?

MR SHARPE: Which?

THE CHAIRMAN: The draft invitation to tender document.

MR SHARPE: We don't think so, if only because that

1 documents referred to an end October date. This
2 document, which I'll take to you in a moment, just
3 simply for the note, the transcript reference in the
4 cross-examination, which you may want to refer to
5 eventually, is Day 9, page 119, lines 13 to 15.

6 When this emerged in cross-examination, it certainly
7 occurred to me that we hadn't seen that document, and
8 enquiries were made of Hogan Lovells, who most helpfully
9 late last night produced it with a covering letter.

10 Have you seen the covering letter?

11 THE CHAIRMAN: No.

12 MR SHARPE: You will find it, I believe, in bundle 18, to
13 which I think three documents or so have been added at
14 the end.

15 MR BEARD: It's tab 29.

16 MR SHARPE: Thank you. Perhaps it would be sensible to
17 allow you to read that document. It's quite short. The
18 letter, I mean, just a covering letter. (Pause)

19 THE CHAIRMAN: Yes.

20 MR SHARPE: Before we deal with substantive issues arising
21 from the report very briefly, you might care to go over
22 to the next tab, which I believe is tab 30, which is
23 Shepherd and Wedderburn's letter of earlier this morning
24 in reply and would you care to read it, please. (Pause)

25 THE CHAIRMAN: Yes.

1 MR SHARPE: Well, it's not a very edifying story but it's
2 not my purpose now to dwell on the obvious. We are
3 hoping that further enquiries will be made. It seems
4 improbable, to put it at its lowest, that the receipt of
5 this report in August 2000, some months before the other
6 tender document at the end of October -- so we don't
7 think they are directly related.

8 We think it unlikely this didn't generate some
9 internal correspondence and consideration and evaluation
10 by the income team, Dr Boarer, Holton, Mr Henderson,
11 perhaps Mr Edwards, who my learned friend will be
12 cross-examining on this document, to the extent that he
13 has any knowledge of it at all. Possibly Dr Brooker was
14 involved.

15 So we await that with interest and I know that that
16 will be done diligently and urgently by my learned
17 friends and those instructing them.

18 But the more important point is the point of
19 substance. Perhaps we could go to the report itself.
20 I have actually no intention at all --

21 MR BEARD: Sorry, can I just deal with those issues to do
22 with process? Making submissions on the substance I'm
23 not sure is going to be that productive.

24 MR SHARPE: I don't intend to make any submissions.

25 MR BEARD: I'm sorry. I was going to just deal with the

1 issue to do with the disclosure and what it is that, in
2 the light of the letter we have received this morning,
3 Dwr Cymru could do, really, as a matter of practicality.

4 THE CHAIRMAN: You mean what is the exercise that you are
5 now carrying out?

6 MR BEARD: Yes, what we can now do because I thought that
7 might assist the Tribunal.

8 THE CHAIRMAN: I think it would be better to wait to see
9 what else comes out, if anything, from that exercise and
10 then we will be able to consider --

11 MR BEARD: I think there are two things to just bear in
12 mind. First of all, I'm very happy to give an account
13 of why this wasn't picked up on disclosure fully, which
14 was fully carried out. I think it's important to stress
15 that the disclosure statements that have been provided
16 set out precisely what has been done and that it has
17 been a proper disclosure exercise undertaken.

18 The second is that Mr Sharpe has referred to further
19 enquiries being made. In the letter from Shepherd and
20 Wedderburn, there is a review of all Dwr Cymru records
21 in relation to stand-alone costs. Clearly that's not
22 going to be feasible --

23 MR SHARPE: Ashgrove stand-alone costs.

24 MR BEARD: Whether or not it is Ashgrove stand-alone costs
25 or not, it's the scope of the review. We are very happy

1 to go back this afternoon and spell out what we can do,
2 rather than discussing it now, but I don't think
3 I should leave the Tribunal with a sense that a complete
4 open-ended review of all Dwr Cymru documents could be
5 sensibly undertaken in the time available.

6 Obviously looking at board minutes and LCE papers,
7 that's fine, going back through the material of Ms Cross
8 and Mr Henderson, if it hasn't already been reviewed for
9 these sorts of purposes, again, there is no issue in
10 relation to that. So we can certainly constructively go
11 to that.

12 THE CHAIRMAN: What I think the Tribunal would expect to
13 happen now is some kind of discussion between
14 Hogan Lovells and your client to work out how it is that
15 this document did not come to light previously, what
16 could have been done differently to bring it to light
17 and then consider whether, if that extra thing had been
18 done, or is done now, there may be other documents that
19 come to light.

20 MR BEARD: As I say, we will identify why it wasn't picked
21 up on disclosure and then see what steps would have been
22 required and whether there are other proportionate steps
23 that could be taken aside from that. Certainly.

24 THE CHAIRMAN: Yes.

25 MR SHARPE: I don't think it's necessary to dignify that

1 with any reply. It's blindingly obvious what has got to
2 be done.

3 May I take you to the report very briefly at bundle 19, tab 57?

4 THE CHAIRMAN: Yes.

5 MR SHARPE: It's only a couple of paragraphs. The title
6 "Non-potable assets study", date August 2000. Hyder
7 Consulting Limited, I have no direct knowledge, I assume
8 they were related to Hyder, which was, I think the
9 parent company at the time. So unless I'm told
10 otherwise, this is an in-house consulting operation.
11 I make nothing of that point at all, just to give you
12 some coordinates.

13 May we go quickly to 1.1, in "Introduction" we see
14 it was:

15 "Hyder Consulting was commissioned by Hyder
16 Utilities to collate information concerning the supply
17 of non-potable water within Wales."

18 We also see that Hyder Utilities staff had close
19 involvement thought the project, and use was made of
20 their knowledge. It would come as no surprise to me,
21 madam, if my learned friend Mr Cook asked Mr Edwards
22 which staff were involved in relation to that.

23 Over the page you see a table giving customers'
24 references, region and supply. This has been
25 appropriately redacted, but we see the very first one is

1 Ashgrove, and that's our matter with Albion as customer,
2 the year 2000. And we see the others, but we have no
3 details of them.

4 But this represents, as I understand it, the
5 totality of distribution assets, only distribution
6 assets, in Wales.

7 If you turn over to 1.2, "Methodology", we see that
8 this document was created as part of the tariff-setting
9 exercise for potable and non-potable water for its
10 customers, and the tariffs are based on the average
11 costs of supplying that water, taking into account the
12 marginal costs and the assets used to deliver that
13 water.

14 I cannot make any sense of that. It either takes
15 account of average costs or it takes account of marginal
16 cost, or it takes account of assets used to deliver that
17 water. But all three represents a sort of belt and
18 braces and something else. But one can only presume
19 that this methodology wasn't conjured up by the
20 consultants out of thin air, it was what they were told
21 to look at.

22 Then the task is:

23 "[To quantify] the assets used to deliver water is
24 vital in setting accurate tariffs that will also be
25 competitive in future. In addition to the standard

1 tariffs, there are a number of customers that are
2 supplied with potable and non-potable water via
3 a bespoke distribution network. In these cases it is
4 possible to use a de-averaged tariff based on the asset
5 value of that specific network."

6 Once again, it is likely that is what they were told
7 and knew, and this is the basis of their work.

8 Then it says:

9 "Identifying the non-potable assets from the
10 de-averaged tariffs is a time consuming activity."

11 Then we come on to the very point that my learned
12 friend I think was cross-examining Dr Bryan on, and that
13 was the inadequacy of the AIS data, and it was the
14 purpose of this study to fill the gap. And the
15 calculation, to take it up to the last paragraph:

16 "The average of non-potable tariffs is also
17 dependent on identifying the non-potable assets. At
18 present, all non-potable assets are categorised as raw
19 water assets on Hyder Utilities' asset information
20 system. [That] includes many kilometres of intake main
21 used to supply water treatment works from source and
22 which are attributed with the production of potable
23 water and should, therefore, not be included in the
24 non-potable tariff calculations."

25 We know from the very first paragraph that tariff

1 calculations were ongoing and indeed we have seen that
2 they were planning to do this for October 2000 because
3 that's -- my understanding -- when the scheme of charges
4 would be presented for approval by Ofwat, done on an
5 annual basis.

6 One last point. If I may take you to three pages
7 from the end of this document, the bottom of document
8 goes through each non-potable asset one by one,
9 beginning with Ashgrove. And it's not necessary to take
10 you to that, but what you see in this chart --

11 THE CHAIRMAN: Which page are we at, please?

12 MR SHARPE: Mine isn't yet ... 7274. And you will
13 appreciate I had this before it was paginated. Do you
14 have it? 7274.

15 THE CHAIRMAN: Yes.

16 MR SHARPE: It's three pages from the end.

17 THE CHAIRMAN: I don't know why it has come out like it has.

18 MR SHARPE: It's not appropriate for me to take you to the
19 detail of it, but I simply want to indicate its
20 importance because this represents each of the assets
21 under examination.

22 If I just take you to -- I think it's the fourth
23 column from the right under the heading "Pipe value".
24 Do you have that?

25 THE CHAIRMAN: Yes.

1 MR SHARPE: I think at the bottom you see "Ashgrove".

2 THE CHAIRMAN: Yes.

3 MR SHARPE: We believe this to be the MEAV value of the
4 assets for each non-potable distribution by reference to
5 the locality. In other words -- do you have it?

6 THE CHAIRMAN: Yes.

7 MR SHARPE: Yes. So whereas the AIS dealt with historic
8 data, as my friend submitted was inappropriate for
9 tariffing, this is the MEAV valuation, which, as the
10 methodology indicates, was indeed appropriate for
11 tariffing and was obviously prepared at the instigation
12 of Welsh Water for that very purpose.

13 In summary, what does this document do? What this
14 document does is provide stand-alone, locally specific
15 asset valuations for bulk, non-potable distribution.
16 This information was in the hands of Welsh Water in
17 August 2000, some considerable time before the
18 application for common carriage was made.

19 In other words, it was not necessary to deal with
20 global averages when they had -- and we now know they
21 had -- specific accurate data produced by their own
22 people on local asset valuation. Therefore, all they
23 would need to complete the jigsaw would be accurate data
24 on non-potable partial treatment. Put the two together.

25 We know that work was in handled. We know that they

1 thought the 30 per cent figure wasn't robust. We know
2 it emerged, but only in 2003 when it was slashed from 30
3 to 15 per cent -- you may recall my showing you that
4 evidence -- three years later and well after the common
5 carriage was issued.

6 What do we do with it? We are lucky enough to have
7 Mr Edwards giving evidence, and he will be examined as
8 best he can on this evidence. We don't have
9 Mr Henderson, Mr Holton, Dr Brooker, and we understand
10 that. I had thought whether it would be sensible to
11 recall Mr Williams, but to put no finer point on it,
12 Mr Williams couldn't even remember who his finance
13 director was. I suspect this would be so far below his
14 range of responsibilities and detail that I'm not
15 entirely sure it would be worth the Tribunal me calling
16 him.

17 However, my learned friend did cross-examine
18 Dr Bryan on the question of asset values, and this was
19 done in the context of the Ofwat disclosure. You will
20 see from the Shepherd and Wedderburn letter that it is
21 our belief that this information should have been given
22 to Ofwat as it was directly relevant, directly relevant,
23 to the section 26 application when they expressly
24 requested stand-alone asset values.

25 I do not know, but we have not seen this document

1 before and my understanding is we have seen everything
2 that was disclosed to Ofwat at that time. I infer from
3 that, subject to correction, that it was not given to
4 Ofwat in 2001 or thereafter. Moreover, it is very
5 likely, as relevant, that it should have been disclosed
6 in subsequent tribunal proceedings. My friend saw fit
7 to cross-examine Dr Bryan. I have asked Dr Bryan
8 whether, if requested by the Tribunal, he would be
9 prepared to assist the Tribunal in giving evidence in
10 relation to this document and its importance and
11 relevance to this case. He is willing to do so --

12 THE CHAIRMAN: Yes. We are not here redoing the earlier
13 proceedings, as to whether this was an abusive price.
14 It is accepted that it was. I'm not, therefore, quite
15 sure what the relevance of Dr Bryan's evidence as
16 opposed to matters that you can raise in submissions
17 would be.

18 MR SHARPE: I'm in your hands, madam. Plainly this is
19 directly relevant to what they knew and when they
20 knew it.

21 THE CHAIRMAN: Yes.

22 MR SHARPE: And of course Dr Bryan can't really comment much
23 on that.

24 THE CHAIRMAN: No, quite.

25 MR SHARPE: But if the Tribunal needs assistance as to its

1 importance, which in many respects is obvious, then
2 Dr Bryan is the only person who can speak to that and be
3 cross-examined. But if the Tribunal is content, then
4 I'm very content not to inflict yet another examination
5 on him.

6 THE CHAIRMAN: Let's see where we get to with how Mr Edwards
7 can help us with this.

8 MR SHARPE: Thank you.

9 THE CHAIRMAN: I notice on the front page of the study it
10 says that the report has been prepared in accordance
11 with terms and conditions of appointment for the
12 non-potable assets study, on the title page at the
13 bottom.

14 MR SHARPE: Indeed so.

15 THE CHAIRMAN: I don't know whether anyone has looked for
16 those, or whether those might also be on Ms Cross'
17 system, but I just raise the point.

18 MR SHARPE: Perhaps, madam, you might prod my friend and
19 give him a useful point of departure.

20 THE CHAIRMAN: Yes. In the meantime, let's continue with
21 Mr Edwards.

22 MR PAUL EDWARDS (continued)

23 Cross-examination by MR COOK (continued)

24 THE CHAIRMAN: Let's proceed with Mr Edwards.

25 MR COOK: Mr Edwards, good morning.

1 Mr Edwards, could you open up bundle 4 to tab 121?

2 Could you go to schedule C, which is at page 852.

3 A. Yes.

4 Q. If you recall, yesterday I produced a sheet of paper
5 which was my attempt to explain what you had done in
6 calculating the FAP, and the first step I had said there
7 was you had calculated the whole company average cost as
8 all the income received from sales of water, divided by
9 the volume of water sold. Do you recall that?

10 A. I recall your sheet, yes.

11 Q. If we go to the middle of the page, you will see, just
12 below the table -- just below the implicit table -- the
13 description there of what had happened, in which you
14 said:

15 "The whole company average cost of water service is
16 calculated as all the income received from sales of
17 water, divided by the volume of water sold."

18 That, of course, was the description I suggested to
19 you was what you had done and you said that wasn't
20 right. So, just to be clear, the explanation that you
21 put forward in the document that was going internally
22 and was going to Ofwat and ultimately went to Albion was
23 wrong, was it?

24 A. That wasn't all of the income received, no. Wrong.

25 Q. So you weren't making clear the fact that you were

1 excluding the Elan Valley bulk supply income?

2 A. That was not clear, no.

3 Q. And you equally weren't making clear that when you
4 looked at costs, you would also exclude some categories
5 of cost from that?

6 A. I think, because we had used a proxy, the income as
7 a proxy for costs, then -- it wasn't clear that we
8 hadn't excluded costs, but we used income as a proxy for
9 costs, rather than costs themselves.

10 Q. So if we go to schedule D, because you looked at costs
11 from what's called the ABC document --

12 A. That's right.

13 Q. -- in order to split up costs, so you had excluded some
14 categories from that allocation, hadn't you, in order to
15 come to those splits, you said yesterday?

16 A. That's correct, yes.

17 Q. Again, that's not made clear?

18 A. That's not made clear, no.

19 Q. If you can keep that document open because we will be
20 coming back to it, could I ask to you turn in bundle 16,
21 I'm afraid, tab 2. This is Welsh Water's Special
22 Agreements Register for the years 1999/2000, and we can
23 see at the bottom left:

24 "Bulk supply exports."

25 And I believe WSHBSE5, which is the penultimate bulk

1 supply export entry, that would be the Elan Valley
2 supply, would it?

3 A. I presume so as well.

4 Q. And that's recorded as being 122 million metres cubed of
5 water a year?

6 A. Yes.

7 Q. So by far and away the biggest supply that Welsh Water
8 had at the time?

9 A. Certainly, yes.

10 THE CHAIRMAN: Is that potable or non-potable?

11 MR COOK: That's raw water.

12 A. We supplied it straight from the reservoirs. Elan
13 Valley and Severn Trent have got their treatment works
14 next door, so it's the draw-off tower of the reservoir.

15 Q. Mr Edwards, so that was the income in relation to that
16 you excluded. I won't ask you to do it on your feet,
17 but I have done the mathematics because we can see the
18 revenue, and the revenue, which we see in, several
19 columns across, "Revenue actual", which was slightly
20 over 4 million at the time, and I have done the
21 calculation and that came to 3.4p per metre cubed in
22 relation to what was effectively a water supply, as in
23 a raw water supply, and that was very much consistent
24 with what you calculated the average cost of water to be
25 in your table -- if we go back now to bundle 4,

1 tab 121 -- what you calculated the cost of water to be
2 for the business as a whole, didn't you? You see this
3 at page 850? The resource was calculated at 3.9?

4 A. Similar figure, yes.

5 Q. So this was some completely uncommercial deal; it was
6 actually at the time broadly consistent with the cost of
7 water itself, wasn't it?

8 A. The numbers were the same, yes.

9 THE CHAIRMAN: You presumably, then, took out the volume of
10 water from the calculation as well as --

11 A. That's correct.

12 THE CHAIRMAN: -- the prices for the water?

13 MR COOK: If we could ask you to turn to schedule D, which
14 is the calculation of the split across, across water
15 resources and treatment, which you showed as being the
16 total of 220 million. It's under the "Total" entry at
17 the bottom of the table.

18 A. Yes.

19 Q. You were doing a split of costs, but if we look above,
20 it actually included an operating profit element -- do
21 you see that -- just above the subtotal entry, about six
22 lines above, an operating profit of 44 million, roughly?

23 A. That's correct, yes.

24 Q. Yes. So effectively this ended up being a sort of
25 residual element, though the costs were, give or take,

1 176 million and the operating profit would be a residual
2 element in that?

3 A. That's correct. It was the balancing figure, once you
4 take all other costs off the total.

5 Q. So in that context you were treating effectively all of
6 the profits that the company made as associated with the
7 water supplies you included in this -- all the profits
8 the company made from water as being associated with the
9 supplies taking place that you included within this, and
10 not associated with things like the Elan Valley supply,
11 which you excluded?

12 A. That's correct. It's the implied profit from the
13 220 million income.

14 Q. So while you were trying to give the impression in your
15 description -- you were describing this as a whole
16 company average -- it was in fact anything but,
17 wasn't it?

18 A. It wasn't the complete whole company average, no.

19 Q. And that was something that you were not making clear in
20 the report at all, were you?

21 A. It's not clear in the report.

22 Q. Now, we went through yesterday what I suggest were some
23 of the errors in the report. What cross-checking did
24 you do in order to check that the figures you were
25 coming to were realistic?

1 A. I think one of the other documents has got some analysis
2 based on work that Mr Taylor had done in the mid 90s to
3 see what figure he had come up with to see if they were
4 the same ballpark figures, the same percentage split.

5 Q. Which other document are you referring to? I'm afraid
6 I can't help you with what you are because I'm not sure
7 I have seen such a document.

8 A. It could be the one I sent to Julie Griffiths. Is that
9 near here?

10 Q. You are referring to the one sent to Julie on
11 20 February. That would be at bundle 4, tab 132.

12 A. On one of my analysis sheets which shows this figure
13 there is handwritten notes which show a sensitivity
14 cross-check.

15 Q. Yes, I believe 881 is being suggested.

16 A. Page 881? Sorry.

17 Q. Yes. No, it's not. I apologise. That's not ... we
18 will come back to that, Mr Edwards, if I can see if we
19 can find that.

20 THE CHAIRMAN: 881, is that Dr Bryan's handwriting?

21 MR COOK: I believe it's likely to be Dr Bryan's
22 handwriting.

23 In terms of what you were doing, as we saw
24 yesterday, you were working out resource, you were
25 working out treatment, you worked out the bulk

1 distribution figure. Wouldn't the obvious thing to do
2 be to look at the other residual element, which was the
3 local distribution figure?

4 A. In terms of looking at local distribution for what
5 reason?

6 Q. Just for effectively seeing if all the numbers added up
7 to the right figure at the end. Wouldn't that be the
8 first figure to look at? You produced three numbers,
9 and there is a residual element, which is local
10 distribution. So wouldn't it be sensible to look at
11 that and see if that ends up being a realistic number at
12 the end of that process because it's the residual? If
13 it doesn't add up to the right number, clearly there is
14 something wrong with the methodology.

15 A. Do you mean if I added that to all the other numbers; is
16 that what you are saying?

17 Q. Yes.

18 A. I think that's the way the calculation worked. I'm
19 sorry, I'm not sure what you are getting at.

20 Q. If we go to bundle 4, tab 125, we can see actually you did do what
21 it was I was asking you about, which is look at the
22 other element of this. It said effectively the potable
23 price includes four elements: resource, treatment, bulk
24 distribution, and then the fourth one was local
25 distribution. And obviously only the first three of

1 those are relevant to the calculation you were doing for
2 common carriage. We can see here you have done the
3 final step of looking at what the local distribution
4 cost arising from your methodology comes to. Do you see
5 that there as being 28.7p?

6 A. Yes.

7 Q. We have seen from Mr Henderson's work, and it follows
8 from the Large Industrial Tariff, that the local
9 distribution cost was in fact 39.1p. Do you remember
10 that figure?

11 A. Is that the work that was called "network access
12 prices"?

13 Q. It appears from that but it's simply the difference
14 between the potable standard tariff and the top band LIT
15 price.

16 A. You said 39.1?

17 Q. 39.1.

18 A. If I remember yesterday, that was the result of Paul's
19 methodology which included the MEAs set at the wrong --
20 sorry, using MEAs wrong.

21 Q. It didn't, because that number is simply the difference
22 between the potable standard price and the top band LIT,
23 isn't it? We can go back to that --

24 A. Is this figure in my documents? The 28.7 or the 39?

25 Q. We can show you where the 39 comes from, if that would

1 assist, if we can go to bundle 2, tab 16. I apologise,
2 it's the wrong reference. It will be bundle 2. Give me
3 a moment just to find the right document. (Pause)

4 So it's tab 15, is the reference.

5 A. The Large Industrial Tariff?

6 Q. Yes.

7 A. Yes.

8 Q. This is when what Mr Henderson was doing. The
9 difference between the equivalent local distribution was
10 the difference between the price for water -- if you go
11 to page 283 -- paid by consumers, which at that time was
12 84p, and the price for water paid by the top band LIT
13 users, wasn't it? That was the fundamental difference
14 between those two numbers.

15 THE CHAIRMAN: So that was the difference between 84.08
16 and --

17 MR COOK: The relevant number would actually be --

18 THE CHAIRMAN: Oh, it would be a mixture of 62,790 and the
19 57.65.

20 MR COOK: On these figures it would a difference between
21 the 84p and a figure which included, yes, the two. And
22 we see what that figure would be at page 292,
23 Mr Edwards.

24 So the average cost per metre cubed is 46p compared
25 to the volumetric charge for consumers, which at that

1 time was 84p. So that's that point and, of course, this
2 was a couple of years earlier. The local distribution
3 difference was 38p, and when Mr Henderson did his work,
4 39.1p was the figure he came to. But that was nothing
5 to do with MEAVs; that was simply the direct difference
6 between the top band LIT price and the retail tariff for
7 normal consumers, for potable water, wasn't it?

8 A. Thank you for reminding me. I believe that's correct,
9 yes.

10 Q. Yes. If we go back to bundle 4, tab 125 we can see that
11 effectively the residual element in your methodology,
12 the one you had calculated, came to 28.7p compared to
13 that 39p, 39.1p, that was the local distribution cost
14 based on the potable tariffs. That was something you
15 were presumably aware of, and it showed immediately,
16 didn't it, that there was a problem with your
17 methodology, because you had ended up knocking off 10p
18 from the cost of the local distribution?

19 A. I can't remember doing that analysis at the time.

20 THE CHAIRMAN: You can't -- sorry, go on.

21 MR COOK: Madam Chairman, if you had a question, please.

22 THE CHAIRMAN: What analysis? You can't remember thinking
23 that the 28.7 was different from the previous 39 figure?

24 A. Yes, I can't remember comparing the two figures.

25 MR COOK: You said yesterday you were very much aware of the

1 fact there had been the changes in the various numbers.
2 There had been a change in the resource number, there
3 had been a change in treatment and a change in bulk
4 distribution compared to your work and Mr Henderson's.
5 So you presumably were also aware of this change that
6 had taken place in the local distribution number?

7 A. I think the analysis I was referring to yesterday was
8 looking at the numbers coming out of the model. So
9 therefore -- I can't remember looking at the local
10 distribution.

11 Q. You clearly did.

12 A. In the way you suggest, sorry. I obviously calculated
13 for this email, but not for comparative purposes.

14 Q. If you don't carry some form of comparison, how could
15 you be confident in the results that you were producing?

16 A model doesn't produce realistic numbers, there is
17 obviously a problem with the model, isn't there?

18 A. That's why the analysis was done, to see whether it was
19 consistent with the numbers that had been created
20 earlier, in earlier methodologies.

21 THE CHAIRMAN: Is that Mr Taylor's work in the mid 90s?

22 A. Yes.

23 THE CHAIRMAN: Just remind me of what that work was.

24 A. It's the work to inform the bulk supply price at Albion,
25 the minded to price.

1 MR COOK: I suggest to you, Mr Edwards, actually it was
2 quite clear, given the most recent work you had had was
3 Mr Henderson, you knew the 39.1p figure fell out
4 automatically, but this told you that there was
5 something off with the results that you were producing,
6 didn't it?

7 A. I can't remember that at the time.

8 Q. Mr Edwards, you can keep bundle 4 open and if we turn it
9 back to tab 121, which is the LCE paper because we are
10 going to be coming back to that. You can put that on
11 one side because I would now like to ask you some
12 questions about the non-potable assets study, which you
13 heard mentioned this morning, which you will find in
14 bundle 18, tab 29.

15 You can turn over the front page, which is a letter
16 from Welsh Water's solicitors, and actually go to the
17 report itself. Looking at the front of this report,
18 it's a report of August 2000, headed "Non-potable assets
19 study". Can you remember having seen this at the time?

20 A. I can't recall seeing this document at the time.

21 Q. Just can you help us: Hyder Utilities and Hyder
22 Consulting, what exactly was their relationship with
23 Welsh Water?

24 A. Welsh Water was transformed into Hyder in the mid 90s
25 and Hyder was a conglomeration or a multi-utility, which

1 included SWALEC and Dwr Cymru and also a consultancy,
2 predominantly Acer, they were called at the time.

3 What happened towards the end of the 90s was that
4 the LiCo, the licence company, was formed and an
5 operating company was formed, and the consulting -- and
6 I think there was a commercial services, which was
7 a billing and income section and IT. So they were all
8 constituent parts of Hyder.

9 Hyder Utilities was the operational area, so it was
10 the operational management of the water and the
11 electricity systems, and Hyder Consulting was what was
12 called Acer. It was rebranded. It was an international
13 consultancy.

14 Q. So Hyder Utilities was effectively the operational wing
15 of Welsh Water?

16 A. That's correct.

17 Q. So I mean, at the time Welsh Water didn't actually have
18 an operational wing of its own at all. So it was
19 effectively all Welsh Water's operations were within
20 Hyder Utilities?

21 A. I think that's correct. I think the company LiCo was
22 a very small company. That was the company that became
23 Glas, which was the 200 members. It was meant to own
24 the licence.

25 Q. Just to be clear, who were you employed by?

- 1 A. Myself, I was in the licence company.
- 2 Q. And in terms of the other names that we know were
3 involved at the time -- Mr Henderson, Dr Boarer -- was
4 everybody employed by the licence company, or would they
5 also be Hyder Utilities?
- 6 A. They were all the licence company.
- 7 Q. But all of the operational staff actually carrying out
8 the business of supplying water to customers, they would
9 all be Hyder Utilities?
- 10 A. Managing the operations would be Hyder Utilities.
- 11 Q. Thank you. Did you know at the time that Mr Henderson
12 had had some analysis already carried out?
- 13 A. It was something that I was reminded when I saw the
14 email trail when I was revising for this. I remember --
15 and that's why I asked Paul about it. So it was
16 something that I was aware of at the time and I was
17 reminded of recently.
- 18 Q. I know you were aware that work was being done. Were
19 you aware that a certain body of work had already been
20 completed?
- 21 A. I'm not sure if I was aware if it was being completed,
22 no.
- 23 Q. And would you have asked to see such a document if you
24 had known it had been done?
- 25 A. I think it's likely I would have, yes.

1 Q. If we go within the report, you can start off at 7250.
2 It's headed "Non-potable assets study", but we see
3 within the report it's only associated with the
4 distribution system. You were aware, of course, that
5 the second part of this would effectively need to be
6 done, which was the treatments works element, weren't
7 you?

8 A. If Paul was going to take it to its conclusion, he would
9 need to understand the watering works, yes.

10 Q. If we go to 7256, which is the section dealing with the
11 individual analysis of different non-potable water
12 systems -- 7256 to 7258, which is a detailed analysis --
13 we can see obviously some attached documents, Ashgrove
14 design, we see at page 7256. There is a reference to
15 some kind of design file having been supplied clearly.
16 And then a detailed analysis, if we go to 7258, in
17 relation to Ashgrove, some analysis of what the water
18 treatment assets are.

19 So it's setting out what all the assets are in the
20 question. You see the analysis there. There is a water
21 treatment works, trunk mains, sludge main. So this is
22 a document that analyses what all the assets are. Do
23 you see that?

24 A. I can see that, yes.

25 Q. And you see in relation to, for example, the trunk main

1 that what it has done is identified specific features
2 associated with it, the length of it, how it's made.

3 This is the kind of information that Welsh Water
4 would have required in order to look at non-potable
5 treatment, wouldn't it? To know exactly what all of the
6 assets were?

7 A. That's correct.

8 Q. I said non-potable treatment. In terms of non-potable
9 supply generally, this was identifying all of the assets
10 was the first step he needed to take, wasn't it?

11 A. That's what Paul was intending to do in this study.

12 Q. As far as we can see, this certainly purports to cover
13 all of the non-potable supplies that were taking place,
14 and I don't need to go through every one with you.

15 Based on what we see was happening with Ashgrove and
16 going through all of the others, that would tend to
17 suggest, wouldn't it, that basically it was a list of
18 all of the non-potable assets that existed and were
19 relevant to non-potable supplies within Welsh Water's
20 region?

21 A. It would suggest that, yes.

22 Q. If we go to the final section --

23 THE CHAIRMAN: Wait a minute. I just don't quite understand
24 that answer.

25 So are there other treatment works not included on

- 1 this list at 7251?
- 2 A. Sorry, the list on which page, please?
- 3 THE CHAIRMAN: 7251.
- 4 A. 7251. The Court Farm system has got a treatment works,
5 it's partially treated, that I know about. I'm not
6 really too confident about some of the rest of them, but
7 I know that Court Farm would have one.
- 8 THE CHAIRMAN: But are these just producing non-potable
9 water or are they producing potable water as well?
- 10 A. From the quick look I have had through it now, I believe
11 these are just looking at the non-potable networks.
12 Court Farm is also a potable treatment water plant and
13 the non-potable treatment bit is separate, so the water
14 source for that is shared with potable water. So
15 I believe this is looking at non-potable systems.
- 16 THE CHAIRMAN: Yes.
- 17 MR COOK: So if we go to 7263, Mr Edwards, we see there in
18 relation to Court Farm that that has been identified as
19 one of the relevant assets to the extent it's dealing
20 with non-potable water. You see that at the bottom
21 there of the page?
- 22 A. Yes, I can see that.
- 23 Q. This looks like a comprehensive list of all assets
24 involved in non-potable water?
- 25 A. It looks comprehensive, but obviously I have only had

1 a short time to look at it. I have no reason to suggest
2 it's not.

3 Q. If we go to 7274, we see this is the table breaking down
4 the different systems, and if we look at the bottom of
5 the page, you see the penultimate entry is for -- it's
6 very difficult to read, but Ashgrove. Can you see that?

7 A. I can see that, yes.

8 Q. And then we look across. Effectively there is
9 a breakdown of the various characteristics of the mains
10 involved, and then four columns from the right
11 a calculation of pipe value, which I believe is about
12 12.3 million in relation to Ashgrove.

13 A. I can see that, yes.

14 Q. And that would be an MEAV figure, wouldn't it?

15 A. I don't know. I would presume it would be an MEAV
16 figure.

17 Q. And that's the kind of information that would have been
18 required to look at the cost of non-potable
19 distribution, wouldn't it?

20 A. Yes, if it's MEA, that's the figure we would have based
21 the cost on.

22 Q. If we can maintain that page open, and if I could ask
23 you to turn to back to bundle 9A, tab 354, this is
24 a document we saw yesterday. This allows us to
25 understand what happened a bit more.

1 A. Sorry, which tab?

2 Q. It's tab 354. It's page 3285. We saw this page, which
3 is headed "Consideration of non-potable prices" and we
4 saw then the breakdown of the non-potable pipe size
5 distribution. It appears the obvious source of the
6 information for this kind of analysis would be the
7 report that had been prepared that we have just seen,
8 wouldn't it?

9 A. I would imagine it either came from the report or the
10 data that was provided to prepare the report.

11 Q. If we look down at the bottom of this -- you can see how
12 this operates, this table. With the exception of the
13 largest figure at the top, which is an enormous main
14 which is dealt with separately, what it does is it adds
15 up a cumulative value going down as you add different
16 elements of the network. We come to a figure at the
17 bottom of, call it 84.6 million roughly. The reason
18 I asked you to keep open the non-potable asset report is
19 we see the figure there, which is not dissimilar, though
20 it's 84.8. So the bottom one.

21 I appreciate there's a close similarity in the
22 numbers. It would appear to indicate, wouldn't it, that
23 the value information that had been used was closely
24 related, whether, as you said, it came from the source
25 materials or whether it came from the results of this

1 report, wouldn't it?

2 A. As a value assumption, yes.

3 THE CHAIRMAN: Just to be clear, you are comparing the
4 84,568,687 at the bottom there with the total pipe value
5 of 84,884,212.71 on --

6 MR COOK: There is obviously a small difference,
7 Madam Chairman.

8 So we see actually the analysis that has been
9 carried out by Mr Henderson is, based on the
10 distribution valuations that he would have received, he
11 is looking at how the distribution values, the value of
12 the assets, relate to the prices that people are
13 being -- the proportion of the water represented by
14 those assets and the prices that people are being
15 charged for that water, isn't it?

16 A. That's the analysis in this table, yes.

17 Q. Yes, and we saw yesterday that the end result
18 effectively is if you have a big pipe and therefore
19 a low unit cost, people are paying small price -- that's
20 the 10p -- and if you have a small pipe and therefore
21 a high unit cost, people are paying much higher price at
22 the time?

23 A. I don't agree with the causality, but that's the way the
24 numbers fall out on this table.

25 Q. That's obviously what the person who is carrying out the

1 analysis is looking at to see, isn't it, looking at that
2 correlation? That's the reason to do that cross-check,
3 isn't it?

4 A. He is looking to see the relationship, yes.

5 Q. And that's the relationship that comes out, isn't it?

6 A. As I said yesterday, I think the middle are all the
7 same, the very high is 10p and the very low is 30.
8 That's the analysis that comes out to me.

9 Q. So Mr Henderson at least appreciated from this that
10 there was this correlation between customers taking
11 large values of non-potable water paying lower prices
12 than customers taking small volumes of non-potable
13 water. That's what the data shows, isn't it?

14 A. I keep saying I think the data doesn't show that.

15 Q. You saw this document at the time. Presumably you would
16 have looked at this analysis. Did you seek to draw any
17 conclusions from it?

18 A. From 3285?

19 Q. 3285.

20 A. I can't remember. No.

21 Q. Because this was something that was fundamental to
22 Welsh Water's approach, wasn't it? If this showed
23 de-averaging, which clearly, if you were paying a
24 different price for large volumes of water than for
25 small volumes of water, by reference to the value of the

1 distribution assets in question, that would not be an
2 averaged approach, would it?

3 A. I think this was being looked at by Paul Henderson to
4 see whether he could justify, as I explained yesterday,
5 the reduction of the standard non-potable tariff to
6 a large non-potable tariff, the same methodology as we
7 had used for the potable LIT, and that's why he was
8 doing this analysis there. I don't think he was doing
9 this to see whether or not there was evidence of
10 de-averaging.

11 Q. But this would have been the kind of analysis that one
12 would need to look at in order to see if there had been
13 de-averaging, wouldn't it?

14 A. I don't think this is the sort of analysis I would have
15 used.

16 Q. It's the kind of analysis that one could use, isn't it?

17 A. It could be used, yes.

18 Q. And did you do any such analysis?

19 A. I did no analysis using this table, no.

20 Q. Did you do any analysis at all as to whether non-potable
21 prices had been de-averaged?

22 A. In terms of looking at numbers and evidence like this?
23 I didn't, no.

24 Q. Because in fact you knew that in practice, Welsh Water
25 was negotiating prices and you said yesterday it

1 effectively took what it could get. So there wasn't in
2 fact some kind of averaging pricing process taking
3 place?

4 A. I think yesterday I was discussing there were elements
5 where we were constrained and we weren't able, because
6 of the existing contracts, to get the value or the price
7 that we wanted, and therefore in those instances we were
8 willing to take a lower price in order to close down the
9 old contracts, put interim contracts in place with the
10 intention of putting the customers, once those contracts
11 have expired, on to the average tariff.

12 Q. You can put away bundle 9A now. The information that
13 we --

14 MR LANDERS: Sorry, just before you do, in that table most
15 of the lines don't have prices. Why would they be
16 missing? You were drawing conclusions from a very small
17 number of prices there.

18 A. I think the only explanation I could give is that some
19 customers would have different sized pipes. I think
20 what Paul may have done here is where he can clearly
21 show a customer relationship with a size pipe, he may
22 have done. So Albion has got a consistent price, but
23 the others would have been shared between different
24 customers. But -- the reality is I don't know, but it
25 would have been difficult on this sort of analysis to

1 clearly pin down which customer took what, which leads
2 me to suggest he wasn't doing this to analyse the price
3 against them. He was just looking at where the
4 customers were to see how far he needed to go down for
5 a large industrial non-potable tariff.

6 MR COWEN: Can I just ask: when you look at the value that
7 you have in the table at 3285 -- it's difficult to read
8 the value of the Ashgrove System. It's 40,735,681.

9 MR COWEN: I just wondered whether that's the cumulative
10 value. You need to take away from that 40 the 28 on the
11 previous line, which gives you the 12 --

12 A. That would be the way I would look at it.

13 MR COWEN: Thank you very much.

14 A. I can put 9A away now?

15 THE CHAIRMAN: As far as you are concerned -- just make sure
16 I understand your evidence -- this table is not aimed at
17 working out whether the price people are paying is
18 related to the size of pipe that they are using, but
19 aimed at working out what size of pipes are used by
20 people buying a non-potable supply so as to work out how
21 much of the cost of the pipe network it's fair to charge
22 to those non-potable users?

23 A. I think it was originally intended to see whether we
24 could justify a reduction from 49p, using this
25 methodology, in the same way as we had used it with the

1 Large Industrial Tariff. So it was a -- this was
2 a method of reducing -- what Paul was trying to see was
3 how much of the mains the large users used compared to
4 the smaller users, to see whether we could take off
5 a substantial -- or justify the reduction from 49 to the
6 26 by taking off the local or small pipes. And what he
7 found out was there wasn't enough value in the small
8 pipes in the non-potable networks to do the same
9 calculation. Therefore, he would have to come up with
10 another way of calculating his large industrial
11 non-potable tariff.

12 THE CHAIRMAN: That's what I don't understand, because
13 underneath the table he says it shows that the
14 non-potable network is composed mainly of large pipes.
15 It could be argued in fact that there is no local
16 distribution network on non-potable supply, so doesn't
17 that then show that it is right to exclude local
18 distribution costs from the non-potable supply?

19 A. I think -- I mean -- what he is saying is they are not
20 included already.

21 THE CHAIRMAN: Oh, I see, because the non-potable pipe
22 system is actually separate from the potable pipe system
23 anyway?

24 A. Yes, so on that logic the 49p wouldn't be reduced by
25 anything because there is no local distribution to take

1 off the 49, and I think that was in the previous paper
2 we saw.

3 THE CHAIRMAN: In a potable supply, how narrow would the
4 pipes get down to being? So here really the smallest
5 one is 10 centimetres.

6 A. I think the connection to the house is smaller than
7 that.

8 THE CHAIRMAN: Yes.

9 A. It's not much more than -- I think it's not much bigger
10 than the pipework in the house. I'm showing my
11 technical knowledge now.

12 THE CHAIRMAN: Yes, I see, okay, thank you.

13 MR COOK: If you can turn back to the non-potable asset
14 report.

15 A. Can I put 9A away again?

16 Q. Yes.

17 A. Yes.

18 Q. The valuations that we saw at 7274 for the non-potable
19 network, that would have provided the information,
20 certainly on the non-potable side, to allow a comparison
21 to be carried out between the costs of potable
22 distribution and the cost of non-potable distribution,
23 wouldn't it?

24 A. It would inform that calculation.

25 Q. So the information was available to do that work. Do

- 1 you recall if it was done?
- 2 A. The information was available and I do not recall
3 whether it was done or not.
- 4 Q. Wouldn't that be an obvious thing to check?
- 5 A. It would be, yes. But I don't recall it being done.
- 6 Q. Is that because everybody knew what the outcome would
7 be, that it would show non-potable distribution was much
8 cheaper?
- 9 A. I don't think so, no.
- 10 Q. Was it something that was vital to do, even if you
11 decided that some form of average was appropriate,
12 because what you ended up doing was looking at the cost
13 of potable distribution, didn't you, because you
14 calculated numbers by reference to the potable tariffs?
- 15 A. I calculated the average price of distribution with
16 reference to the potable -- Paul Henderson calculated
17 with reference to the volumetric potable tariff and
18 I included more numbers in that, so it was a bit
19 different -- the calculation I did.
- 20 Q. But your calculation ultimately tied itself to the
21 potable LIT, didn't it?
- 22 A. It included LIT as one of the elements, yes.
- 23 Q. So ultimately you were looking at something which was
24 a potable distribution price?
- 25 A. I think the -- the step I did was assume that the

1 average price of bulk distribution of potable water was
2 the same as the average price.

3 Q. For all distribution?

4 A. Distribution.

5 Q. So without knowing whether non-potable distribution is
6 cheaper, you do not know whether that comparability is
7 true or not, do you?

8 A. As I said yesterday, the reason of averaging is that you
9 know that certain things in the average are cheaper, and
10 you know that certain things are more expensive, and
11 therefore --

12 Q. But if you are only averaging part of Welsh Water's
13 entire network, so you are excluding basically the
14 cheapest bit of the network, the average you produce is
15 not a company average, is it?

16 A. I'm not sure we are excluding -- you mean the Elan
17 Valley?

18 Q. You are excluding the non-potable part of the network.
19 So effectively you are creating an average that only
20 looks at the expensive part of the distribution network,
21 aren't you?

22 A. I'm not sure I excluded the non-potable part.

23 Q. You are because you ultimately use the potable LIT,
24 which is exclusively potable-based, in order to
25 calculate the distribution price, don't you?

- 1 A. I use the potable LIT as a proxy to determine the cost
2 of the local network, and therefore the residual --
- 3 Q. No, you don't, because you are not looking at the local
4 network at all in your calculation?
- 5 A. But the local network is removed from that calculation.
6 The point of the non-potable LIT is that that
7 calculation was a proxy for what the costs of the local
8 network were.
- 9 Q. In your calculation, you then take the potable LIT
10 figure and deduct -- and we had this yesterday -- the
11 treatment and resources element, and what you are left
12 with is therefore a bulk potable distribution?
- 13 A. That wasn't the intention of doing it. I think you
14 showed yesterday that was the -- when you reworked the
15 maths.
- 16 Q. No, that was what you were doing. That's how you did
17 the calculation and you came to a figure which you
18 called the bulk distribution element. But that was
19 a purely potable figure, wasn't it?
- 20 A. I'm not sure because the original volume and the
21 original costs would have included -- I think would have
22 included the non-potable. I wasn't aware of I was
23 excluding the non-potable element.
- 24 Q. Did you give any thought to it at all?
- 25 A. I can't recall that.

1 Q. Look at this report now. If we go back to page 7255,
2 this is the methodology section. It's the second
3 sentence I wanted to see if you could help us with.
4 It's referring -- the first sentence:

5 " ... Hyder Utilities will need to submit to Ofwat
6 the tariffs of potable and non-potable water ... "

7 So it's talking about the tariffs for both. It
8 says:

9 "The tariffs are based on the average cost for
10 supplying that water taking into account the marginal
11 costs and the assets used to deliver that water."

12 That seems to suggest if they are talking about both
13 potable and non-potable tariffs, that the non-potable
14 tariff takes account of the asset used to deliver that
15 water. Is that right?

16 A. I think this just -- it's a fairly general sentence.
17 Whether that means long run marginal cost, I don't know
18 and the tariff will be based on the assets used to
19 deliver the water, but I can't see how you can draw any
20 other conclusion than that.

21 Q. If you see in the paragraph below, it says:

22 "In addition to standard tariffs, there are a number
23 of customers that are supplied with potable and
24 non-potable water via a bespoke distribution network.
25 In these cases it is possible to use a de-averaged

1 tariff based on the asset value of that specific
2 network."

3 If you could hold that open for a moment and we will
4 go back to bundle 3, tab 59, please, which you remember
5 of course is the MD163 document that we have been to
6 before.

7 Could I ask you to turn in it to a paragraph we are
8 now both very familiar with, which is page 611. The
9 three options that are put there, the first of those,
10 the accounting costs, the book value of the assets to
11 which access is sought. It's clear, isn't it, that what
12 Hyder Consulting is being asked to do is carry out the
13 calculation which paragraph 1 invites, doesn't it?
14 Talking about the asset value of the specific network,
15 ie the book value of the assets to which access is
16 sought. It's clear that's what they are being asked to
17 do, isn't it?

18 A. What's the specific question? Hyder have been asked to
19 do what, sorry?

20 Q. You can see that Hyder are saying it's possible to use a
21 de-averaged tariff based on the asset value of that
22 specific network. And I'm suggesting to you it's clear,
23 isn't it, that the work they have been asked to do is
24 linked directly to what Ofwat has said is an appropriate
25 approach, which is the asset value of the relevant

1 assets, used in a supply?

2 A. I don't see the direct link from that. That's just
3 a statement of fact. I'm not sure what the brief was
4 for this work.

5 Q. We can put away this document now. I just want to
6 quickly go back using, I'm afraid, some of the documents
7 we saw yesterday with the information now that this work
8 had been done. So the work had been done in
9 August 2000.

10 If we go to bundle 3, tab 86, we saw this yesterday
11 but we now know, of course, that there had been a report
12 produced, which had used valuations for the distribution
13 network. So in terms of the cost information being
14 sought here, it would appear that what's left to be
15 done, effectively, the second half of the equation, is
16 looking at treatment works, and that would suggest
17 that's what's being looked at here, wouldn't it?

18 A. I think the treatment works here in the 12 areas would
19 be all treatment works.

20 Q. So it's looking at what you can do in terms of providing
21 some form of comparability between potable treatment and
22 partial treatment?

23 A. It's looking to see what the costs of the large watering
24 works are. I don't think it says what it's going to be
25 used for.

1 Q. We can see the reference, middle of that paragraph,
2 obviously relevant to Ashgrove. So this work is being
3 done in the context of the Albion's common carriage
4 application, which, of course, we see at the bottom of
5 the page as well. So it's not being done for some
6 general purpose. It's being done certainly with an eye
7 on the fact this Albion's common carriage calculation is
8 taking place?

9 A. I accept that, yes.

10 Q. So the treatment works was the second part of the
11 equation in terms of having some idea what the
12 non-potable stand-alone tariff would be, wouldn't it?

13 A. It could be, yes.

14 Q. So that was 24 November. If we go to tab 99 now, the
15 email exchange you had with Dr Boarer on 12 December,
16 and you are suggesting, we see in the bottom email:

17 No information should be given to either Ofwat or
18 Albion.

19 While you respond reasonably to all correspondence.
20 Then Dr Boarer responds -- and this is the fourth
21 line -- agreeing with you:

22 "On this basis getting the appropriate data together
23 asap is essential. I believe Paul (H) is already on the
24 case."

25 So that looks like a link to the work that

1 Mr Henderson is already doing in terms of non-potable
2 information, doesn't it?

3 A. That's the assumption I would make by reading these two,
4 yes.

5 Q. If we go to tab 103, which again we saw yesterday, and
6 the exchange we saw in the middle of the page, your
7 email, Dr Boarer, Mr Holton, saying:

8 "I thought Paul was getting the asset info to
9 calculate a stand-alone non-potable tariff not to look
10 at the company average non-potable element of all
11 treatment works."

12 Looking at that, effectively the only element left
13 for both those jobs was simply the information on water
14 treatment, wasn't it?

15 A. And the resources as well.

16 Q. Yes.

17 A. Yes.

18 Q. And, again, we saw at tab 110 the reference in the LCE
19 paper -- which, again, we are familiar with -- was the
20 outstanding point was -- this is at page 801:

21 "A robust asset value based price for the
22 non-potable portion of the treatment price."

23 Again, a reference to the outstanding bit of the
24 work Mr Henderson was doing?

25 A. Could you point me to that, please?

- 1 Q. 801, the final sentence above "Risks".
- 2 A. Yes, that's correct.
- 3 Q. So this is work that Mr Henderson, it looked like, had
4 started, certainly some time prior to August 2000
5 because he had obviously instructed Hyder Consulting to
6 do the work presumably some time earlier, for them to
7 have completed it in August 2000, and he now had been
8 carrying on with presumably since that period of time,
9 and was still doing?
- 10 A. I believe at the time Paul was looking at calculating
11 the large industrial non-potable tariff, yes.
- 12 Q. Thank you. Could we now turn back -- I said we would
13 come back to it -- to the second LCE paper, which is
14 bundle 4, tab 121?
- 15 THE CHAIRMAN: Is that a convenient moment for us to take
16 our mid-morning break?
- 17 MR COOK: That would be, yes.
- 18 THE CHAIRMAN: We will come back at 11.50 am.
19 (11.46 am)
20 (Short break)
21 (11.56 am)
- 22 MR COOK: Mr Edwards, we were back to bundle 4, tab 121. If
23 we go to page 851 in this, we see that you are using the
24 30 per cent figure for converting potable treatment to
25 non-potable treatment.

1 We know from your answers yesterday that you
2 appreciated that figure was out of date and there were
3 certainly issues with how much work had gone into it
4 originally. Why was it you were still using it in this
5 calculation?

6 A. At the time we had no other evidence that we could use.

7 Q. Mr Henderson had been working on that, we now know, he
8 had been working on non-potable assets since, certainly,
9 August 2000 and seemed to be looking at treatments since
10 November 2000. This is now three months after that.

11 Why hadn't he got anywhere in relation to that process?

12 A. I can't remember. All I can remember is that there was
13 no report coming out of that work that I could use for
14 this analysis.

15 Q. Was there any indication of how long it would take?

16 A. I don't recall that.

17 Q. Did you ask for it?

18 A. I can't recall asking for it. I would have checked
19 because I knew this number was an old number, so I would
20 have checked to see whether there was a more recent
21 number.

22 Q. You agreed there was no practical difficulty with
23 carrying out that work because Welsh Water did it
24 eventually two years later, didn't it?

25 A. Yes, that's correct.

1 Q. And it came, of course, to a number that was around half
2 the number you were using. It came to a 15.2 figure.

3 You are familiar with that?

4 A. I believe so, yes. Is this the decision or the referred
5 work?

6 Q. No, the 15.2 number was the number that Welsh Water
7 submitted in the context of the non-potable list.

8 A. I recognise that number.

9 MR BEARD: That response from Mr Cook is not correct. It
10 was also the material submitted in the context of the
11 decision of Welsh Water.

12 MR COOK: Whose decision was it to proceed with using
13 a number that you knew was out of date, potentially
14 inaccurate?

15 A. I think we had no choice, but I'm not sure who would
16 have made the decision. Paul Henderson and myself were
17 aware of the number and would have discussed it with
18 Dave and probably with Jackie, but I don't think there
19 was a choice because there was no other number there.

20 THE CHAIRMAN: That's Dave Holton?

21 A. Dave Holton, yes. Sorry, Mr Holton.

22 MR COOK: But you don't remember having any idea what the
23 timescale was for producing more up-to-date work?

24 A. I have no idea, no.

25 Q. And you can't help us at all as to why it had taken so

- 1 long to do it?
- 2 A. I can't, I'm sorry.
- 3 Q. This, of course, if we go back, was the actual paper
4 that was prepared for presentation to the LCE, or to the
5 board. In the earlier LCE paper, which we have seen
6 before -- I hope you do not need to go back to it -- of
7 course you had flagged up the fact that the 30 per cent
8 figure was out of date and there were issues about its
9 reliability. Why wasn't that something that you were
10 identifying for the assistance of the LCE on this
11 occasion?
- 12 A. Which paper was the other paper you commented on?
- 13 Q. It was the paper that was at bundle 3, tab 110. It was
14 the one we saw that went to the board in January 2001
15 and that identified the issues with the 1995 figure.
- 16 A. I'm not sure why it was not carried forward to this
17 paper, but if the board had already seen the
18 information, they would have been aware of it.
- 19 Q. The reality is that this was a paper that you knew would
20 be seen, certainly the details in the background would
21 be seen by Ofwat and Albion, didn't you? You knew that
22 was likely to be the case?
- 23 A. The -- my intention was to release the appendix to
24 Ofwat, yes.
- 25 Q. And that was the reason why you weren't identifying in

1 it the fact there was a clear problem with one of the
2 principal numbers used. You didn't want Ofwat to know
3 about that issue?

4 A. Ofwat would have known the derivation of the 30 per cent
5 as well. So it wasn't a deliberate removal of it to
6 avoid letting people know.

7 Q. It wouldn't have known the derivation because it doesn't
8 say within this anywhere where the figure has come from,
9 and Ofwat would have no way of knowing whether it is
10 indeed a figure that was five years out of date, or
11 whether in fact you have done the work that week based
12 on up-to-date data and it's an up-to-date correct
13 figure?

14 A. The purpose of releasing this information to Ofwat was
15 to discuss it with them and we would have told them at
16 that meeting the intention, which is clear in subsequent
17 emails, is that we were going to go and visit Ofwat,
18 I think Julie Griffiths and Paul Dixon had discussed it,
19 to discuss what we were doing in this paper with Ofwat.

20 So there was no intention to keep it from them.
21 That was my belief -- is what would have happened once
22 we had taken this paper to the LiCo.

23 Q. Taking out the explanation with the 30 per cent figure
24 from this paper, you said the LCE would have been aware.
25 The reality is unless it's flagged again they would have

1 no way of knowing that that is not a figure that you
2 have now had clarity on -- again, this it's not a modern
3 figure, will they?

4 A. If they have seen the original calculation of
5 30 per cent, we are not saying it's a different number.

6 THE CHAIRMAN: Why wouldn't they assume that you have now
7 done the work and, in fact, it has also come out at
8 30 per cent?

9 A. I think we would have told them -- if this was newer,
10 better data, we would have told them that. But they
11 could have assumed that.

12 MR LANDERS: Did you go to the LiCo?

13 A. I don't think I did for this paper, no.

14 MR COOK: In terms of who would go to the LiCo, I mean, just
15 be clear. The Licence Company Executive, effectively
16 that is all of the executive directors of Welsh Water;
17 is that right?

18 A. I think there were some senior managers on there as well
19 at the time because it was in the state of flux between
20 the old Dwr Cymru and the new Glas. There would have
21 been senior managers as well as executive directors.

22 Q. So in terms of the board, the non-executive directors of
23 the board wouldn't sit on the LiCo?

24 A. No.

25 Q. So Mr Williams and Dr Brooker would have been on both?

- 1 A. Yes.
- 2 Q. Was this something that you discussed with Mr Williams,
3 the 30 per cent figure, at this time?
- 4 A. It would have come up in conversation when I was
5 explaining the paper to him.
- 6 Q. Can I ask you now to turn to tab 121, page 848, the front page of
7 the paper. It says at paragraph 5.2:
- 8 "The indicative price released to Albion Water was
9 a simple estimate produced to give Albion Water an idea
10 of the likely price. The calculation has now been
11 revisited and a firm price has been calculated."
- 12 That wasn't explaining, was it, that there had been
13 certainly a quite significant change in the methodology
14 that you were using?
- 15 A. No, that doesn't explain that.
- 16 Q. Wasn't that something that it would be important for the
17 board to know, that the price they had approved
18 previously and issued as an indicative price was
19 calculated on a different basis from the new price?
- 20 A. I'm not sure if Dave -- Mr Holton -- or Mr Williams
21 could have told them at the board. It wasn't included
22 in the paper.
- 23 Q. The reality was you were trying it give the impression
24 that there was consistency in your pricing approach,
25 weren't you, and that's the reason why you weren't

- 1 making clear there had been a change in methodology?
- 2 A. I don't think we were trying to show we were being
3 consistent. I think we were being consistent. We just
4 updated the methodology that Paul had used with my
5 methodology, by changing the starting point. So I don't
6 think -- I don't think we were trying to imply that.
- 7 Q. The reality was that in terms of the information that
8 was going to go to Ofwat or Albion, you didn't want to
9 give the impression that you were changing your
10 methodology because that would suggest that you weren't
11 being consistent with the past, wouldn't it?
- 12 A. No.
- 13 Q. There is also a discussion, we see here in
14 paragraph 5.3, in the final sentence. It says:
15 "It is intended that these schedules are discussed
16 commercially in confidence with Ofwat."
17 In terms of confidentiality, I mean, what was the
18 confidentiality issue associated with this work?
- 19 A. I think it was to make sure Ofwat were comfortable with
20 the work before we released it to Albion Water.
- 21 Q. So the confidence was only to make sure that Ofwat
22 didn't tell Albion. There wasn't actually anything
23 intrinsically confidential about the information, was
24 there?
- 25 A. Not that I was aware of.

1 Q. Effectively what you want was the opportunity to make
2 submissions to Ofwat before they heard submissions from
3 Albion?

4 A. That's right, yes, on our price.

5 Q. On the basis that you had managed to persuade Ofwat that
6 (inaudible) very difficult to get Albion to change their
7 mind, wouldn't it?

8 A. I think what we are looking for is confirmation from
9 Ofwat that they were happy that our method was
10 consistent with methods that they had seen and approved
11 before, before showing it to Albion Water, because,
12 I agree, our hand would be strong if Ofwat had indicated
13 they were happy with the tariffs.

14 Q. And you wanted them to form that view without the
15 benefit of any opposing point of view, didn't you?

16 A. We were concerned what would happen once we revealed the
17 data to Albion. Therefore, we want to discuss it first
18 with Ofwat. That was the traditional route over the
19 last ten or 11 years we would have been used to that,
20 Ofwat would have been the first point of call. Ofwat
21 were driving the competition agenda. Therefore, that's
22 the traditional route we would have taken.

23 Q. And then paragraph 5.5, we see there the reference to
24 the level of prices, meaning Albion Water's common
25 carriage application, is not economic. So that would,

1 of course, have assuaged the board's concern about
2 common carriage damaging Welsh Water's revenue,
3 wouldn't it?

4 A. I think it's the opposite: it's warning the board that
5 on release of prices, we were likely to get a challenge
6 from Albion Water.

7 Q. We saw the original analysis that you produced. Who
8 analysed that within Welsh Water?

9 A. How do you mean?

10 Q. I mean, Mr Henderson, Dr Boarer, Mr Holton. To what
11 extent were they involved in analysing the work that you
12 had done?

13 A. I would have gone through the work with at least
14 Paul Henderson, I think. I would have discussed it with
15 Jackie and with Paul and probably with Jeff Williams,
16 Mr Williams, as well.

17 Q. So effectively in terms of the decision tree, who would
18 be making the decision that this should go to the board?

19 A. Ultimately it would be Mr Williams, it was his paper.

20 Q. But prior to that. I mean, presumably it would be
21 Dr Boarer or Mr Holton?

22 A. I recollect some meetings with Mr Williams and Mr Holton
23 without Dr Boarer. Jackie wasn't there. So it's just
24 as likely that Mr Holton would have recommended it to
25 Mr Williams.

1 Q. You think it was Mr Holton?

2 A. I was either Mr Holton or Dr Boarer.

3 THE CHAIRMAN: Just remind me where Mr Holton is. Is he
4 junior to you, or senior to you?

5 A. He was senior to me. Around this time he was, earlier
6 on in the process, reporting to Dr --

7 THE CHAIRMAN: He was senior to you but junior to
8 Mr Williams?

9 A. That's right.

10 THE CHAIRMAN: Was he on a level with Dr Boarer?

11 A. I think when the process started he was reporting to
12 Dr Boarer, and some time afterwards he then moved up and
13 reported direct to Mr Williams.

14 MR COOK: Can you just help us? Mr Holton, does he still
15 work for Welsh Water?

16 A. He does not, no.

17 Q. Dr Boarer?

18 A. She does not, no.

19 Q. When did they both leave?

20 A. I'm not sure of the exact date. I would guess around
21 2005. We tend to have severance around the time of
22 periodic reviews. So I would guess around there, but
23 I'm not exactly sure.

24 Q. If we turn back it bundle 3 --

25 THE CHAIRMAN: Can I just ask you: Dave Holton, did he have

1 sort of similar qualifications to yours?

2 A. No, he was more a commercial manager and operations
3 background.

4 THE CHAIRMAN: Just looking back, what's your sense of how
5 great a grip he had on the numbers that you were
6 crunching for the company?

7 A. I think in terms of the arithmetic, he may have been
8 aware, but in terms of the background, the regulation
9 background, he wouldn't have been very aware of that at
10 the time. At the time the regulation department, who
11 I talked about -- probably the first day I was on, there
12 was four people. At that time, all of those had left.
13 The other key regulation people, which was Chris Jones
14 and Nigel Annett, had also left. So I was the only link
15 to the past there, and Paul Henderson had picked up the
16 tariff mantle a couple of years ago. So between
17 Paul Henderson and myself, we were the specialists in
18 the team.

19 THE CHAIRMAN: As far as questions about -- we have been
20 going through should you cut out the Elan Valley water
21 supply from the figures; should you use MEA values; how
22 you pull out the proportion figures from the ABC tables.
23 If anybody, who did you discuss those sorts of judgment
24 calls, as it were, with, or was that something you came
25 up with yourself?

1 A. I think in terms of developing the model, it would be
2 between myself and Paul Henderson. So Paul did the
3 original analysis, I analysed what he was doing and then
4 from that I went back to what Dennis Taylor was doing to
5 try and make sure that we had the link to the past.

6 THE CHAIRMAN: Was Dennis Taylor someone that you discussed
7 this with or you were just looking at the output of
8 his --

9 A. Dennis had left by that time.

10 THE CHAIRMAN: And Mr Henderson was the same level of
11 seniority as you?

12 A. I think so, yes.

13 THE CHAIRMAN: So it was really up to the two of you to come
14 up with the model and make those sorts of decisions
15 about how the model was going to work?

16 A. At the detailed level, yes.

17 THE CHAIRMAN: Well, at the detailed level, but in your
18 discussions with Dr Boarer and Mr Holton, would you go
19 through with them those sorts of decisions about the
20 construction of the model?

21 A. I think so. we would do it at the level that I have
22 shown you here, and previously I had had a spreadsheet
23 which I would have gone through what I had done.

24 THE CHAIRMAN: Right. And to what extent did they have
25 sufficient background to challenge any of those

1 decisions that you had taken?

2 A. I think in terms of very technical knowledge, they
3 wouldn't have that, but in terms of curiosity, they
4 would be wishing to understand why we had made certain
5 decisions.

6 THE CHAIRMAN: Right. Okay, thank you.

7 MR COWEN: Is this subject to any typical sort of financial
8 control or finance director oversight?

9 A. The regulation department previously was under the guide
10 of the finance director, including regulation at the
11 time. But at that time there was -- the finance
12 director, Gedwyn Miles, would not have had a regulatory
13 remit. So the regulatory remit because of the nature,
14 was probably with Dr Brooker.

15 THE CHAIRMAN: Yes, thank you.

16 MR COOK: Just to be clear, you said the regulatory remit
17 was with Dr Brooker. So Dr Brooker would also have been
18 somebody looking closely at exactly what you were doing;
19 is that right?

20 A. Yes, he would be aware of what we were doing. He would
21 take an interest.

22 Q. We talked about Mr Holton. Mr Holton, of course, his
23 job description made himself competition manager. I
24 appreciate he had other responsibilities, but he was
25 competition manager as well, wasn't he?

- 1 A. That's correct, yes.
- 2 Q. So he was the person with sort of primary responsibility
3 for determining the competition legality of what was
4 being done?
- 5 A. Compliance with competition, yes.
- 6 Q. And if Dr Brooker was the individual who sort of had
7 overall regulatory responsibility for the company, he
8 would want to sort of have that talked through with him,
9 wouldn't he?
- 10 A. I think he would have either spoke through with
11 Dave Holton or with Jeff, yes, he would want to know the
12 sort of level of -- you know, the importance of this
13 document. He would want to know the details behind it.
- 14 Q. But he wouldn't have talked to you about it?
- 15 A. He may have done.
- 16 Q. Sorry, just to be clear, sorry, you may have talked to
17 Dr Brooker about this? You are not sure?
- 18 A. I may have discussed it with Dr Brooker, yes.
19 Dr Brooker wouldn't have gone through the hierarchy. If
20 he had wanted to know some detail, he would have come
21 and spoke to me.
- 22 Q. You can't remember?
- 23 A. I can't remember discussing it with him.
- 24 Q. But Mr Holton or Mr Williams --
- 25 A. Definitely, yes.

1 Q. Is it perhaps fairer to suggest that if Dr Brooker had
2 wanted to understand exactly what was going on he would
3 have talked certainly to Mr Holton, rather than
4 Mr Williams alone?

5 A. Probably, yes, I think Mr Williams would have gone in in
6 any discussions with Mr Holton.

7 Q. Can I just ask you to turn back to bundle 3, tab 37,
8 please? Sorry, before we come to this document, I have
9 a couple of supplemental questions in relation to the
10 LCE payment. We don't need to go back to it, simply
11 knowing it's there.

12 There hadn't been any form of stand-alone
13 non-potable comparison carried out, had there, by that
14 point?

15 A. I don't believe there had.

16 Q. Despite the fact that was part of the compliance
17 checklist that you had prepared?

18 A. That's correct.

19 Q. Whose decision was it to produce this without carrying
20 out that comparison?

21 A. I am not sure it was a decision. I think the checklist
22 that we saw yesterday I produced in order to guide my
23 development of the statement of principles and the
24 network access code, and I don't remember seeing --
25 using it for this work. I believe what would happen is

1 I would have filed it with the network access code
2 filings and when I came back to this work, I wouldn't
3 have picked it up again. Therefore, I wasn't using the
4 checklist.

5 Q. You prepared it for Mr Holton?

6 A. I prepared it for myself.

7 Q. You said Mr Holton asked you to prepare that yesterday.

8 A. Yes, I prepared it for myself, so to ensure what when
9 they produced the statement of principles for March and
10 the network access code, that we had included everything
11 that we were supposed to.

12 Q. So you think nobody gave any thought to having
13 a stand-alone check carried out?

14 A. I can't remember it because we didn't have the data at
15 the time, the analysis at the time.

16 Q. So if you are now at bundle 3, tab 37, this is a letter
17 that appears out of order and it appears out of order
18 because you see it's dated on its face 29 January 2000,
19 and it should be dated 2001. That's the reason why the
20 letter is out of order.

21 So this was a letter from Ofwat saying, "What's
22 going on?" effectively. It's asking: why has an
23 indicative figure not been provided? Of course, it's
24 slightly behind the loop because an indicative figure
25 was provided back in mid-January.

1 Can we go back to bundle 4, tab 122, this was
2 Mr Holton responding to Ofwat's letter we have just
3 seen. Go to the fourth paragraph, and it's referring to
4 the negotiations that have been taking place with
5 Albion Water. You see that in the fourth line:

6 "Current negotiations with Albion Water are being
7 conducted on a commercial basis with the full knowledge
8 of Ofwat. Our position is and always has been to
9 conduct these negotiations in an open and communicative
10 manner."

11 Just to be clear, the open and communicative manner
12 did not extended to providing any real explanation at
13 all of the way in which Welsh Water were approaching
14 pricing, other than simply the mantra of average
15 pricing?

16 A. In terms of pricing at that time, that's correct.

17 Q. So it really wasn't right to say that it was an open and
18 communicative process, was it, to that extent?

19 A. I think negotiations around common carriage are more
20 than just on price. There were a lot of operational
21 issues and other legal issues, so therefore we were
22 engaged in those. There was a very complicated deal
23 with the bulk supply with UU and we were engaged in
24 that. Therefore, the open communication is that we were
25 engaging on all aspects of common carriage with Albion.

1 At that time we hadn't got the price, therefore we
2 hadn't revealed it.

3 Q. Hadn't revealed anything about price formulation at all,
4 had you, apart from the words "average price"?

5 A. Not at that time, no.

6 Q. If you go to bundle 4, tab 127, it's a further email response from
7 Mr Holton to Ofwat on 9 February. It's Mr Holton saying
8 in the third paragraph:

9 "We are refining our work on the price and
10 cross-referencing the work against figures and documents
11 you have already received and agreed. I hope to get
12 board approval for the price within the next week, board
13 agenda allowing, and then be in a position to issue a
14 price to Albion Water with a copy to yourself."

15 Mr Holton would presumably be setting out an
16 accurate statement of what his plans were at that time
17 in terms of getting board approval, wouldn't he?

18 A. I think that was the intention, yes.

19 Q. And that must, therefore, have been a reflection of the
20 fact this was something the board would want to see
21 before it was issued?

22 A. I think this price, we recognised, was the common
23 carriage price for access to all of our networks.
24 Therefore, we deemed it appropriate and competition was
25 very high on the agenda of Ofwat at the time.

1 Therefore, it would be appropriate to go to the board.

2 Q. If we go to bundle 4, tab 128 now, this is a letter from
3 Julie Griffiths to yourself of 15 February 2001 and she
4 is referring to a telephone call she had with you that
5 day saying:

6 "I'm pleased to hear that you have finally reached
7 agreement on your access price figure and methodology
8 after your board meeting."

9 Presumably you would have been accurately setting
10 out your understanding at the time to Ofwat,
11 wouldn't you?

12 A. In the phone call, yes.

13 Q. So looking at that, it does appear that it would have
14 been discussed at a board meeting that day, doesn't it,
15 that day or the day before, perhaps?

16 A. Whenever the board was, yes, that's correct.

17 Q. So the issue had been discussed at the November board,
18 hadn't it?

19 A. I think we established that yesterday, yes.

20 Q. It had been intended to be discussed at the December
21 board meeting, but there wasn't a price at the time?

22 A. That's correct.

23 Q. Do you recall that? Yes? It had been discussed in
24 January when a decision had been taken to approve the
25 issue of the indicative price. Do you recall that?

- 1 A. Yes.
- 2 Q. So Welsh Water were now going to be issuing the final
3 price. Can you help us as to why there is no reference
4 in any board minutes to the final price being approved
5 by the board?
- 6 A. I can't help with you that, I'm afraid.
- 7 Q. Looking at all this, it looks very clear, doesn't it,
8 that it was approved by the board before it was issued?
- 9 A. If that's what I said on the phone, then I see no reason
10 why it wouldn't have been approved at the board.
- 11 Q. Do you recall being told it had been approved?
- 12 A. I think I wouldn't have said to Ofwat it had been
13 approved by the board if I hadn't been told that.
- 14 Q. I asked if you recall --
- 15 A. Sorry, I beg your pardon. I don't recall, no.
- 16 Q. The only reason for the board not to record that
17 decision was because they didn't want to be associated
18 with something that they knew was excessive. It's
19 a logical conclusion, isn't it?
- 20 A. No.
- 21 Q. What other reason would there be for the board not to
22 record its decision to issue a price which was going to
23 become Welsh Water's common carriage price?
- 24 A. The previous board minutes had not recorded that the
25 price -- what had been approved. Therefore -- I never

1 saw the board minutes, but I don't believe it was that
2 reason.

3 Q. So we see from this letter that approval had been given.
4 Why was a final price not offered to Albion immediately
5 then?

6 A. Because we were going to discuss it with Ofwat.

7 Q. Even though you knew that Albion had been waiting for
8 four and a half months already?

9 A. Yes.

10 Q. Whose decision was that?

11 A. That was the process we were going to go through from
12 the earlier emails, that we intended to discuss it with
13 Ofwat. So I think that was the process we had agreed as
14 a team. Dave Holton would have approved it.

15 Q. If we go to 4, tab 130, the exchange that you had with
16 Mr Liesner, who I believe was an economist, wasn't he?

17 A. That's right, yes.

18 Q. At NERA?

19 A. At NERA, yes.

20 Q. We see in your email, which is at page 873 -- you are
21 asking about the calculation. You see the final bit of
22 that email exchange -- well, there's a bit above that as
23 discussed on the phone and responds by Monday, but above
24 that it says:

25 "I intend to release the calculations only to

1 Ofwat. I don't see why we should release them to
2 Albion."

3 Why were you saying that?

4 A. I think that was in terms of timing. I think we were
5 going to release the calculations to Ofwat and then
6 going to discuss them with Albion, with Roddy Monroe.

7 Q. You are saying:

8 "I don't see any reason why you should release them
9 to Albion."

10 You said:

11 "I intend to release them only to Ofwat."

12 You are saying you are not going to release them to
13 Albion at all.

14 A. I think at the time -- I think this was basically: can
15 you give me your opinion of these, I'm going to release
16 them now to Ofwat, not to Albion. It was not my
17 intention never to release them to Albion. That's one
18 of the reasons I set them out in the way they were, so
19 that Albion could understand the numbers as well. I was
20 confident that Ofwat would be able to understand the
21 numbers. So I was trying to use as many numbers in the
22 public domain so that Albion could understand the
23 numbers and calculation as well and discuss them
24 with us.

25 Q. We can see Mr Liesner's response over the page. He is

1 saying he doesn't see any reason why you:

2 " ... shouldn't go ahead and release the attachments
3 to Ofwat, provided you provide the necessary caveats
4 (see below). As you indicate, this may be only the
5 start of a process of to-ing and fro-ing if your
6 proposed price makes Albion's proposals uneconomic.
7 Most of the information in the attachments is publicly
8 available anyway (or can be reasonably accurately
9 assumed), so I do not see that you are prejudicing your
10 position."

11 That response would suggest, wouldn't it, that he
12 understood they wouldn't be released to Albion at all,
13 and he is saying the information is available. That's
14 fair, isn't it?

15 A. I had asked him if I could release them to Ofwat and he
16 had said yes, and then saying the process of to-ing and
17 fro-ing was discussing it with the parties once Albion
18 had received the price.

19 Q. In terms of the price, nobody was suggesting within
20 Welsh Water that this price was up for negotiation, was
21 it, in terms of Albion?

22 A. That was my intention.

23 Q. How was it your intention? If you had reached
24 a conclusion on the price, how was it up for
25 negotiation?

1 A. I had reached approval on the price and the methodology,
2 and that was for discussion. It was very high level
3 methodology for discussion with Ofwat and Albion.

4 Q. How exactly is it high level methodology?

5 A. Because the granularity of the calculation isn't very
6 great, it's only at very high level because of the time
7 I had to put the price together. And I think in the
8 letter to Julie Griffiths we say that we recognise it's
9 a high level price and that the process of calculating
10 common carriage price is ongoing and we may change the
11 price as we get better information.

12 Q. So this was a recognition of the fact that you were
13 using information that bore very little resemblance to
14 the actual services Albion was requesting?

15 A. I think it was recognising we were using very high level
16 numbers. We hadn't split out at a lower level some of
17 the costs that may be -- that aren't being included. We
18 had made apportionments of the costs, and with a lot
19 more time we could have started building models where we
20 allocated the different elements a lot more correctly.

21 Q. Welsh Water had known about the Competition Act since,
22 presumably 1998, hadn't it?

23 A. I would have thought so, yes.

24 Q. We saw that it had known certainly the importance that
25 Ofwat was placing upon it from November 1999?

- 1 A. That's correct.
- 2 Q. And that Ofwat was saying at that time it needed to be
3 ready to respond substantively to applications for
4 1 March 2000?
- 5 A. That's correct, yes.
- 6 Q. Do you remember that? Why was it effectively a year
7 later that you were still at the stage where you hadn't
8 got together any form of model that was anything other
9 than what you would call a high level model?
- 10 A. I think at the time there was no precedent of common
11 carriage and we were feeling our way, trying to
12 understand what it was. I think that's why we were at
13 that stage -- I'm not sure any other companies had
14 common carriage prices at that time, either.
- 15 Q. Albion had applied four and a half months earlier, back
16 in September. It was more than enough time, wasn't it,
17 to do something that would produce something that you
18 describe as a high level model.
- 19 A. I think four and a half months on its own would be
20 enough time, but given the state of the flux of the
21 company and the availability of staff to do it,
22 I certainly produced what I could to the best of my
23 ability in the time I had.
- 24 Q. Did you tell people that you weren't producing something
25 that you felt comfortable with?

1 A. I felt at the time it was good enough to release. I was
2 not --

3 Q. You seem now to be saying that you recognise that it was
4 imperfect and that more detailed work would be required
5 to produce a more accurate figure?

6 A. I think Dave was -- the team were aware that there could
7 be a more detailed model produced.

8 Q. Did you tell anybody about those concerns that you had?

9 A. What concerns, sorry?

10 Q. You are saying that this was a high level model and more
11 detailed models might produce different numbers. Did
12 you tell people that?

13 A. I can't recall telling people that, but that's what was
14 known. That's why we were doing the extra work.

15 Q. So the team generally knew that there were uncertainties
16 about the high level figures you were producing?

17 A. With the 30 per cent they knew at least with that that
18 there was some concern, which is why we were going to
19 discuss it with Ofwat and with Albion.

20 Q. Now, I understand you were involved in responding to
21 Ofwat's section -- well, put the background, of course.
22 Albion, then, doesn't like the response it gets, it
23 complains, Ofwat starts its investigation. I understand
24 you were involved in dealing with Ofwat's section 26
25 request, made in June 2001?

- 1 A. Yes, I was.
- 2 Q. When you say "involved in dealing with it", what was
3 your role?
- 4 A. Unfortunately this is one of the areas I can't remember
5 at the time. It has been -- I think I would have been
6 involved with the pricing issues, so explaining the
7 model we had used and approach to pricing. So I would
8 have been involved with that.
- 9 Q. So you actually can't remember the extent of your
10 involvement; is that what you are saying?
- 11 A. All I can remember is once we had the section 26 notice,
12 we were called in by the director, a team was formed led
13 by Mr Holton and I remember having at least one visit to
14 London to the lawyers, who were advising us on the
15 submission, and that's my -- all I can recollect.
- 16 Q. So Mr Holton was in charge of it?
- 17 A. Mr Holton was the project manager for our response, yes.
- 18 MR LANDERS: When you say you were called in by the
19 directors, what directors are you talking about?
- 20 A. At the time Glas had taken over. So I remember
21 Mr Annett, Mr Jones, meeting with those two, and
22 probably Mr Brooker would be there as well.
- 23 THE CHAIRMAN: Is that the first time that you had met with
24 that group of people in the context of this whole
25 exercise?

1 A. I think in the context of this, as far as I recall, it
2 was, yes.

3 THE CHAIRMAN: In the context of your work on developing the
4 common carriage price?

5 A. Yes.

6 MR COOK: If we can go to bundle 4, tab 154, can you help us quickly
7 before we look at the request with who else was involved
8 in that team. You said Mr Holton was putting together
9 a team. Who else from Welsh Water was involved?

10 A. The only other person I remember is a gentleman called
11 Simon Coton, who had taken over the role I was
12 doing -- the role I was developing when I did the
13 statement of principles and network access code,
14 Mr Coton came in and did that. After the price had been
15 revealed to Ofwat and to Albion, I no longer worked for
16 the competition team and worked back in regulation.

17 Q. Do you recall if Mr Henderson was involved?

18 A. I don't recall if he was. I can't remember him being
19 there, but I am not sure.

20 Q. But Mr Henderson would have been sort of still
21 working -- did he work for Mr Holton, or did he work for
22 Dr Boarer?

23 A. I think he worked for Dr Boarer and when Dave moved up
24 to work for Mr Williams. I think he would still have
25 worked for Dr Boarer.

1 Q. In terms of Mr Holton's knowledge, he was fully aware of
2 what Mr Henderson had been doing in terms of the
3 non-potable work, presumably?

4 A. I believe he would have been, yes.

5 Q. So he would have been aware of the non-potable asset
6 study we have seen this morning?

7 A. I'm not sure, because I wasn't, I'm not sure if he was.
8 I would have expected him to be aware of it, but ...

9 THE CHAIRMAN: Just wait one moment. (Pause)

10 MR COWEN: If I may -- I don't mean to interrupt -- in 872,
11 which is tab 130, we were just looking at the email from
12 Jerry Liesner. Can I just ask you if you could to read
13 out paragraph 2. It's the third paragraph down and it
14 starts:

15 "I do think that you should make it clear to Ofwat
16 ..."

17 Could you read that out, please?

18 A. "I do think ..."

19 You want me to read it out, sorry?

20 MR COWEN: Please, yes, so that it's recorded.

21 A. "I do think that you should make it clear to Ofwat that
22 the level and structure of these prices reflects our
23 current thinking, that detailed analysis of common
24 carriage pricing is ongoing and that "the company may
25 refine its approach in due course in accordance with the

1 objective of preparing a comprehensive and fair access
2 pricing scheme for all situations." I say this for two
3 reasons. One, other companies are taking a less
4 generous retail minus approach to access pricing, which
5 you may wish to emulate in due course if it does not
6 prove to be unacceptable elsewhere. Two, looking in my
7 crystal ball for a moment, you may come to consider
8 alternative structures for access pricing, in particular
9 formulations based around reservation or capacity
10 charges have can considerable merit in the context of
11 pricing a transportation service and have the potential
12 advantage of being universally applicable across
13 a number of customer classes."

14 MR COWEN: Thank you.

15 THE CHAIRMAN: NERA, was this their first involvement in it,
16 or had they been involved with you as you went along --

17 A. Sorry, not with the common carriage application. NERA
18 had done a lot of work on our tariffs with Dr Boarer at
19 the end of the 90s, and NERA had also helped us with the
20 iDok. So NERA were our preferred economic consultants.

21 THE CHAIRMAN: But would it be fair to say that the points
22 that Mr Liesner was making in this email fed through to
23 your letter to Julie Griffiths at tab 132, page 875 to an extent?

24 A. Definitely some of the points in this email were in that
25 letter, yes.

1 THE CHAIRMAN: Yes. Yes, thank you.

2 MR COOK: Just to be clear, by the look of it this email
3 exchange is taking place after the board has approved
4 the price already?

5 A. That's correct, yes. We had gone to the board and
6 I wanted a final peer review before we did finally send
7 it to -- so it may have been a board request, but it was
8 a peer review I was looking for.

9 Q. So it was sent to the board as, "This is the price that
10 will be our common carriage provision"?

11 A. Yes.

12 Q. And that's the basis on which the board approved it?

13 A. Yes.

14 Q. So the caveat here was something that was suggested
15 after the board had already approved it as being the
16 final price?

17 A. The price that was approved at the board before this,
18 and this was just me saying, "I'm going to provide Ofwat
19 with a series of schedules. Can you have one final
20 check that I've made no howlers?"

21 Q. Unless the Tribunal have any other questions, can you go
22 back to bundle 4, tab 155?

23 A. 155, sorry?

24 Q. 154 we should go to first, which is the section 26
25 request.

1 A. Yes.

2 Q. Would you have seen this document at the time?

3 A. I would have. This was the document that we were
4 discussing with the executive when I was called into the
5 executive.

6 Q. Which parts of it were you involved in responding to?

7 A. I mean, I would definitely have pulled together the
8 analysis that I did in this for the board and
9 (inaudible) access of the price, and I would probably
10 have been involved with the financial elements as well.

11 Q. In terms of financial elements, we can look here at --
12 we start off actually with request 1, please.

13 A. Yes.

14 Q. Which is:

15 "Please provide copies of all documents."

16 It has the usual:

17 "Including without limitations ..."

18 A whole number of categories of documents:

19 "... which relate or may relate directly or
20 indirectly to Albion's request for access to the
21 Ashgrove System... The terms... under which access... would or
22 might be offered ... the methodologies used ... and
23 terms of access under common carriage to any
24 infrastructure owned ... by Dŵr Cymru."

25 What instructions were given to you in terms of

- 1 gathering together that information?
- 2 A. I remember -- if I recall, Mr Coton would have pulled
3 the documents together and I remember giving documents
4 to people. So all of my files would have been put into
5 the response area. So every file there, which is --
6 a lot of documents you see here with my handwriting on
7 would have come from that document collection.
- 8 Q. You know that Mr Holton was obviously still involved
9 because he was in charge of this process?
- 10 A. That's correct.
- 11 Q. Dr Boarer was still at the company?
- 12 A. Dr Boarer was still at the company, yes.
- 13 Q. Mr Henderson was still at the company?
- 14 A. Mr Henderson, was, yes.
- 15 Q. So there is no reason to think any of their information
16 would have disappeared by this stage?
- 17 A. No.
- 18 Q. There is nonetheless a surprising gap in a lot of
19 information which clearly did exist at the time. It
20 appears to suggest that it was no longer available by
21 this stage; is that fair?
- 22 A. I'm not sure why it wasn't sent. I gave all the
23 information I had.
- 24 Q. If we go to request 14, it says:
25 "Please provide a breakdown of the actual costs

1 incurred by Welsh Water in providing the services
2 requested by Albion Water. How do these actual costs
3 compare to costs calculated on a whole company average
4 basis?"

5 That request wasn't a surprise to you, was it?

6 A. I don't think it would have been, no.

7 Q. It's the obvious cross-check, to find out what the
8 actual costs of the supply are, isn't it?

9 A. That's correct, yes.

10 Q. And you knew, of course, from the original guidance,
11 that was how Ofwat was going to look at excessive
12 pricing, by reference to stand-alone costs?

13 A. I would have known that, yes.

14 Q. Presumably you also knew that as a result of that, if
15 the actual costs turn out to be significantly below
16 23.2p, then there is a very good chance there would be
17 a finding of abuse against Welsh Water?

18 A. I think so, yes.

19 Q. We go then to 155, which is the response to question 14.
20 You said you were involved in the financial bits. Would
21 you have been involved in this response?

22 A. I can't remember. However, this to me is definitely
23 Mr Taylor's work. This is the way he would have
24 presented it, and I believe I would have been the only
25 person who would be able to find it. So, therefore,

1 I conclude that I would probably have done this piece of
2 work.

3 Q. If we look at what's provided here. I mean, what we
4 have is in the bottom two thirds of the page under the
5 heading "The 1995/1996 analysis is presented in the
6 tables below", and then that sets out the analysis which
7 had apparently been done back in 1995/1996. Then the
8 bit above explains what's being done here. It says:

9 "In 1995/1996 a breakdown of local costs for the
10 Ashgrove System was prepared in the context of the bulk
11 supply agreement requested by Albion Water Limited.
12 This resulted in local costs being estimated at 19.6p
13 ... for the bulk supply ... [which] is equivalent to
14 16.1p ... for the common carriage services now
15 requested."

16 Then:

17 "Welsh Water has no reason to believe that this
18 breakdown would not still be broadly accurate today.
19 Allowing for inflation and K factors this figure would
20 be close to 20p ... for 2000/2001."

21 Then I believe that's the common carriage figure,
22 isn't it, the 20p? We see above it's 19.6 is the bulk
23 supply and 16p is common carriage. So the 20p figure,
24 presumably, since it's being compared to the access
25 price, that's being suggested as a common carriage price

- 1 as well, isn't it?
- 2 A. Without calculating, I assume that's the total less the
3 bulk purchase price; is that correct?
- 4 Q. That's the 19.6 is the bulk.
- 5 A. Yes.
- 6 Q. And we see above 16.1 is common carriage, and you are
7 now saying allowing for inflation and K factors, this
8 figure would be close to 20p now. That seems to be
9 suggesting, since it's being compared to the access
10 price, that that's also a common carriage price?
- 11 A. I think what it looks like it has done is the 19.6 minus
12 the 3.5 is -- that's the, presumably, 16.1?
- 13 Q. That is, yes.
- 14 A. The 16.1, so therefore that would -- I assume that
15 figure they are using there is what this is suggesting
16 the common carriage price on a -- on the basis that
17 Dennis has prepared here.
- 18 Q. Then it's saying:
19 "Allowing for inflation and K factors this figure
20 will be close to 20p now."
21 That 20p figure looks like the 16 per cent figure
22 uplifted for inflation?
- 23 A. That's what I would expect to see, yes.
- 24 Q. So it's a common carriage figure?
- 25 A. Yes.

- 1 Q. This was the work --
- 2 THE CHAIRMAN: What, then, is the combined access price?
- 3 MR COOK: That's the FAP.
- 4 THE CHAIRMAN: What's the relationship between the 20p and
5 the 23.2p?
- 6 MR COOK: It's a comparison.
- 7 A. I think the 23.2p is the figure that I had released as
8 the first access price, and that has been compared to
9 the 20p, which is the calculation of this. So it's just
10 comparing the two to see how much different the first
11 access price is to the stand-alone, or the stand-alone
12 as it's represented here.
- 13 THE CHAIRMAN: I see.
- 14 MR COOK: So it's saying: based on these numbers, uplifted
15 with inflation, the local common carriage price would be
16 about 20p, which compares reasonably with the first
17 access price?
- 18 A. That's what this is saying, yes.
- 19 Q. So the statement has been made:
20 "Welsh Water has no reason to believe that that
21 breakdown would not still be broadly accurate today."
22 Do you recall what work was done in order to make
23 that statement?
- 24 A. I don't, no.
- 25 Q. But presumably work would have been done before

1 Welsh Water was in position to make that kind of
2 statement to the regulator?

3 A. I'm sorry, I can't remember.

4 Q. So Welsh Water has been asked for a breakdown of the
5 actual costs incurred. What attempt did you make to
6 check Welsh Water's records for up-to-date cost
7 information?

8 A. As I say, I can't remember pulling this together, but
9 I think this would have been produced because they
10 hadn't got the information to produce that up-to-date
11 figures. But I can't remember, I'm sorry.

12 Q. But we have seen before the operating cost figures for
13 the water treatment works, why would that not have
14 been -- I appreciate that's not every single operational
15 cost involved, but in response to the question of the
16 actual costs incurred, that would presumably be an
17 obvious answer to part of the question, wouldn't it?

18 A. It would have been an obvious answer, yes.

19 Q. Why wasn't it provided?

20 A. I can't answer, I'm afraid.

21 Q. In terms of the costs incurred, since you are looking at
22 distribution and we now know that back in August 2000
23 there had been a calculation carried out for the value
24 of the pipeline at Ashgrove, why wasn't that document
25 provided in response to this question?

- 1 A. I don't know.
- 2 Q. Basically it was the key document in response to the
3 distribution side of the question, wasn't it?
- 4 A. It would have helped this, yes, but I'm not sure --
5 suggesting maybe Paul Henderson, Mr Henderson, wasn't
6 involved with this, but I'm not sure why it wasn't used.
- 7 Q. In terms of the asset register, that, as you say, didn't
8 include any AV figures, but it did show ongoing capital
9 expenditure. Again, that would have been a relevant
10 document to provide in answer to this question,
11 wouldn't it?
- 12 A. It would have been, yes.
- 13 Q. Did you make no attempt to look for those kind of
14 documents?
- 15 A. I can't remember.
- 16 Q. In terms of the availability of information within
17 Welsh Water, had you tried, that information would have
18 been readily available, wouldn't it?
- 19 A. The information -- the information to replicate a lot of
20 this would have been available.
- 21 Q. And so presumably, before you were in a position to make
22 the statement to the regulator, Welsh Water has no
23 reason to believe it would not still be broadly accurate
24 today, those kind of checks would need to have been
25 carried out?

1 A. I'm not sure what happened. I'm not sure how we arrived
2 at that statement. It would be sensible to do checks,
3 yes.

4 MR COWEN: Can I just ask: do you have a process by which,
5 you know, a section 26 notice comes in and then goes
6 through certain checks and balances, other functions,
7 a compliance function maybe?

8 A. We didn't have a compliance function, no, so it would
9 have been set up on response. Dave would have been
10 targeted with producing a process himself, and we got
11 Denton Wilde Sapte at the time to advise us on the
12 application, or the legal process to go through. So we
13 didn't have a set process.

14 MR COWEN: Thank you.

15 MR COOK: If we look at the breakdown of the costings that
16 are put forward in that document, we see at the bottom
17 of the page various breakdowns:

18 "Infrastructure renewal ... return on capital ...
19 bulk purchase ... operating costs ... rates."

20 Then if we go over the page, we see effectively the
21 final big cost that's added on, which is management
22 on-cost at 6.2p. So without that management on-cost,
23 the figure would have come to 13.3p. Do you see that?

24 A. Yes, I see that.

25 Q. So effectively the management oncost adds a whole

- 1 50 per cent to the price being calculated here?
- 2 A. That's correct, yes.
- 3 Q. In reality it was, by some margin, far and away the
- 4 biggest cost entry in this calculation, wasn't it?
- 5 A. That's probably what I would expect to see, yes.
- 6 Q. So in terms of carrying out any checks on it, that would
- 7 have been the first item to carry out some checks on,
- 8 wouldn't it?
- 9 A. I think the first thing I would have checked on this is
- 10 the easy numbers to figure is the volumes of
- 11 Shotton Paper, but it would have been one of the numbers
- 12 to check, yes.
- 13 Q. I mean, taking the volume of supply at Ashgrove, 6.2p
- 14 equates to around £600,000 for the total volume being
- 15 supplied to both Corus and Shotton Paper. I'm not
- 16 asking you to test my arithmetic. Take it at face
- 17 value. If it's wrong I will no doubt be told at some
- 18 point by the other side.
- 19 A. Thank you.
- 20 Q. There was simply no category of management oncosts
- 21 coming in anything close to £600,000 associated with
- 22 this system, was there?
- 23 A. I don't believe that management oncosts refers to
- 24 management. As I have said yesterday, we have a large
- 25 amount of shared and common costs and they would all be

1 in that management oncost. What we have got and
2 analysed here are the local costs at a very low level,
3 and then the 6.2, which is why I said I was not
4 surprised it is so high is all the other costs, the cost
5 of IT and all the other things shared amongst all of our
6 customers, and what Mr Taylor would have done is
7 apportioned it fairly to them.

8 Q. You say "all the other things", but looking through the
9 categories of cost, it has telemetry, so all the costs
10 associated with the operation of the system itself,
11 hasn't it?

12 A. What I meant by the IT function was the things like
13 running the finance systems, running the big mainframes,
14 not the actual IT of running the water treatment works.

15 So all of those costs are not allocated directly to
16 local cost centres, the local cost centres are there for
17 local managers to allow them to budget, and then all the
18 other costs are held centrally and shared across the
19 cost centres, when we do this type of analysis.

20 Q. Effectively these are central office functions, aren't
21 they, we are talking about?

22 A. Central support functions.

23 Q. In 2006 -- we can turn to bundle 6. You can keep this
24 open, Madam Chairman, we are staying with this document.
25 I'm showing a comparison document to the witness.

1 THE CHAIRMAN: Okay.

2 MR COOK: We can go on to bundle 6, tab 241.

3 A. Do I need -- I have got bundle 3. Did you need that?

4 Q. Bundle 3 can go for a moment.

5 A. I'm running out of space. 241?

6 Q. Yes.

7 A. Yes.

8 Q. And then if you go to the front of this, just so that

9 I can explain what this document is. This was a witness

10 statement filed by Christopher Jones, the finance

11 director of Welsh Water, in the liability proceedings.

12 And he had been asked, we see, if we go down to 1926 --

13 or Welsh Water had been asked and Mr Jones had

14 responded, to look at the stand-alone costs of the

15 Ashgrove System in 2000 and 2001.

16 A. I think on 1920 Mr Jones mentions the D21 document as

17 well. Why he believes it's of limited assistance to the

18 Tribunal.

19 Q. This was Mr Jones trying to step back from that

20 document, isn't it?

21 A. He is trying to do a different analysis, yes.

22 Q. He is not trying to do a different analysis, he is

23 actually trying to do an analysis of the stand-alone

24 costs involved.

25 So paragraph 28, 1926, he is doing a stand-alone

1 analysis -- the stand-alone costs of the
2 Ashgrove System, so exactly what Welsh Water had been
3 asked to do in response to the section 26 notice.

4 That's right, isn't it?

5 A. He has calculated the stand-alone costs of the
6 Ashgrove System in 2000, yes.

7 Q. If we look down, we can see the penultimate entry, as
8 opposed to the third line from the bottom. He
9 calculates the business management and overhead. The
10 amount is about £100,000, roughly 1.1p per metre cubed.

11 A. I can see that, yes.

12 Q. How was it that the figure of six times that was
13 included in the D21 document provided to Ofwat?

14 A. I think first of all it's not relating to the same
15 costs.

16 Q. How is that not relating to the same cost?

17 A. I think it gives you -- in 29 it lists a number of items
18 that aren't included there, which includes the IT and
19 the administrative support. So there is a lot of the --
20 what you call the office functions aren't included in
21 that number.

22 Without seeing what was in the six and what was
23 this, I cannot explain exactly what the differences are,
24 but if this is the stand-alone cost for that system
25 being run as a stand-alone system, it wouldn't include

1 all the overheads of a very large company and therefore
2 would be -- because it is such a smaller system, it
3 would be a lot cheaper.

4 Q. Mr Jones says -- you refer to those other items. He
5 says those items are not readily calculable. So if
6 there weren't readily calculable after Welsh Water had
7 had a number of years to look at it in the course of the
8 tribunal proceedings, are they ones you would have been
9 able to readily calculate back in 2001?

10 A. I think they would be readily calculable in the way
11 Dennis had done them on a sort of average basis.
12 I think he is not doing it at this page.

13 Q. It's not a question of what Dennis had done previously;
14 this was a document that you were putting forward to
15 Ofwat as you:

16 " ... had no reason to believe it would not still be
17 broadly accurate."

18 So you would have had to have engaged in
19 a verification process to make that assertion. It's not
20 a question of what you had done previously. What did
21 you do in 2001 to say that Welsh Water could make that
22 statement?

23 A. I cannot recall what I did.

24 Q. The 6.2 figure was the old one. It was the one back
25 from 1995/1996, and we saw that Welsh Water had told

1 Ofwat:

2 "Taking account of inflation and K factors, the
3 overly figure would equate to 20p ... "

4 At that time, which was an increase of 25 per cent.
5 So you were broadly suggesting that the figures in the
6 table below had increased by 25 per cent, which would
7 lead to management oncost of nearly 8p per metre cubed
8 or three quarters of a million pounds for the whole
9 system. What attempt did you make to check that figure
10 was being realistic?

11 A. I can't remember.

12 Q. You knew that this was ultimately going to be a document
13 that would allow Ofwat to test the stand-alone costs of
14 the system, which would be, Ofwat had said, its primary
15 check against the validity of the FAP. How could you
16 possibly have clarified those kind of figures when
17 Mr Jones, when he actually did the work five years
18 later, came to a figure that was 1.1, as opposed to an
19 implied figure here of 8p for management oncosts?

20 A. I think Mr Jones is doing a different piece of work here
21 to what Mr Taylor did there.

22 Q. It's not a different piece of work, it's answering
23 exactly the same question: What are the stand-alone
24 costs of the system, and in one you are coming to
25 a figure that's eight times higher than the other. What

- 1 work did you do to clarify the numbers?
- 2 A. I can't remember.
- 3 Q. The reality is you knew without that management oncost
4 Ofwat was going to find this was an abusive price,
5 didn't you?
- 6 A. I can't remember. I put this in at the time because
7 that was all we had. I can't believe, if we had
8 anything else, I would have put a piece of work in from
9 five or six years ago. Therefore, the only conclusion
10 I have is that that is all we had and there was no --
11 nothing in my mind to say whether or not that management
12 oncost would or wouldn't --
- 13 Q. You say if you had anything else; we know you had
14 operating costs from the printouts from the system, we
15 know there was the August 2000 reports. So you did have
16 something else.
- 17 A. Welsh Water had something else.
- 18 Q. Which you would have asked for.
- 19 A. I would have asked if we had anything else that we could
20 use to do this, and I can't remember doing it but
21 obviously we didn't.
- 22 Q. Obviously you did because we know you did.
- 23 A. Sorry, obviously Welsh Water did but I did not have
24 access -- I wasn't able to access it.
- 25 Q. The reality is that this was a number that was being put

1 forward to justify a price that everybody knew at
2 Welsh Water was completely unjustifiable, wasn't it?

3 A. No.

4 Q. Madam Chairman, that's probably a convenient moment.
5 What I have left are some questions on the calculations
6 of damages or the elements that go into that:
7 non-potable supply ...

8 MR LANDERS: I'm not clear: in terms of the management costs
9 and the overall management cost, how did you determine
10 that out of the overall management costs for the entire
11 company, the amount that should be allocated to this
12 particular contract should be the number in the
13 schedule?

14 A. In the schedule on 969?

15 THE CHAIRMAN: Yes.

16 MR LANDERS: Yes. On 969 you say it's 6.2, which is, as it
17 has been pointed out, £600,000 in total. How did you
18 decide that all the management costs for the company,
19 600,000, was allocatable to Ashgrove?

20 A. I'm not sure how Dennis would have done it, I'm sorry.

21 MR LANDERS: Do you know what percentage it was of the total
22 company figure?

23 A. Not at the time, no.

24 MR LANDERS: 600,000 sounds as if it's a very large
25 proportion of total management overheads.

1 A. I know that the actual local costs that we keep at cost
2 centres aren't a very big proportion of costs. So there
3 is a large amount of smearing. So there is a lot of
4 central budgets. So all the IT is held in one budget,
5 all the infrastructure renewals is held in one budget,
6 which is why Dennis has had to do a likely figure for
7 the infrastructure renewals there.

8 MR COOK: That's separate, just to be clear. That's
9 a separate item.

10 A. I think Mr Jones -- there is analysis in one of
11 Mr Jones' witness statement which shows the split of the
12 actual local costs that they can allocate and then the
13 attributable costs. So ...

14 MR LANDERS: Can I just ask: you have got a total amount of
15 costs for the company, you can allocate them to
16 particular projects or particular systems in terms of so
17 much per metre of water or so much per number of people
18 employed or so much -- there are all sorts of bases. Do
19 you know what sort of bases were used in Welsh Water at
20 this time that might have led to this allocation?

21 A. I'm not sure at that time. I know we did a study not
22 long after that to look at activity-based costing and
23 I remember being in a meeting where it was discussed,
24 because we had joined together with SWALEC and when we
25 split up into Hyder Utilities and LiCo, what the idea of

1 the Hyder Utilities was to get some multi-utility
2 economies of scope, and what they were trying to do
3 there is allocate out the activity-based costing.

4 It was quite far advanced but in the end it was
5 decided not to go ahead. I think one of the reasons was
6 SWALEC said they had tried to do it and they couldn't
7 get any evidence or it didn't add any value because the
8 level of the smearing -- people spend most of their time
9 filling in timesheets. So, therefore, it wasn't done on
10 an activity-based basis and Dennis would have used
11 something like volume of water or an MEA value to
12 allocate it. But it wouldn't have been done on a per
13 head basis.

14 MR LANDERS: When this was submitted to Ofwat by the team
15 that you talked about that was assembled, were there any
16 accountants in that team?

17 A. I don't recall if there was. I'm trying to think.

18 MR LANDERS: You're not an accountant?

19 A. I'm not an accountant, no. I'm not aware of any
20 accountants being involved.

21 MR LANDERS: Okay.

22 A. I can't find the Chris Jones report but it's in the
23 evidence, the split that shows -- it's a pie chart and
24 shows actually how much of our costs are actually very
25 clearly attributable to cost centres and how much is

1 smeared.

2 MR COWEN: When you talk about smearing, what you are
3 actually saying is it's a non-causal relationship; it's
4 simply some form of arithmetic allocation or
5 a percentage or something at that time?

6 A. Yes, it's either based on volume or --

7 MR COWEN: So, rather than saying, as I said earlier, this
8 is highly discretionary, it's a question of judgment?

9 A. Yes.

10 MR COWEN: Thank you.

11 THE CHAIRMAN: There it's being expressed as a charge per
12 cubic metre of water.

13 A. Yes.

14 THE CHAIRMAN: Was that a common way of expressing this
15 charge?

16 A. I think, because Dennis would have been doing it to
17 justify the bulk supply price, that's how he would have
18 presented it.

19 THE CHAIRMAN: Right. But if you grossed up that figure, so
20 that the total costs bear the same relation to these
21 costs as the total volume of water bears to the water
22 supplied through the Ashgrove System -- do you
23 understand what I'm talking about? If you say, "Well,
24 this means the Ashgrove System bears a certain value of
25 those costs expressed as 6.2p per metre cubed," if you

1 then gross that up to work out what then is the total
2 amount of costs if it was being apportioned per metre
3 cubed, do you get to something which approximates to the
4 actual total costs?

5 A. I'm not sure because there is so much of the averaging
6 going on that -- it is all depends on the -- how much of
7 the oncosts and how they are allocated, I think, which
8 is what Mr Jones is trying to do in his paper.

9 MR LANDERS: This comes to 6.2 per metre cubed.

10 A. Yes.

11 MR LANDERS: If you multiply 6.2p by the total volume of
12 water that Dwr Cymru sold --

13 A. Right.

14 MR LANDERS: -- would you get to an overheads figure that
15 looks reasonably close to what the real overheads
16 figure is?

17 A. For the company?

18 MR LANDERS: Yes, please.

19 A. I would expect that to be the case. That would be the
20 way I think Dennis would have calculated it. He would
21 start with the total figure and divide it by the volume
22 to get the 6.2.

23 MR LANDERS: Even though Ashgrove presumably requires less
24 management time than a customer in Cardiff?

25 A. I think so, yes. That the way the averaging works in

1 terms of this. It's based on the volume of water you
2 take, rather than the activity that you cause us to
3 undertake. So that's exactly right.

4 MR LANDERS: One more question. Going back to your earlier
5 evidence, in terms of the time which it took to send
6 stuff to Albion and so on and so forth, were you ever
7 given a timetable which said, "We must respond to Albion
8 by this date, we must get a price fixed by this date",
9 or did it just creep along?

10 A. I wouldn't say it crept along, it was more driven by the
11 board. We were conscious that we had to get a price.
12 We were conscious that we would find it difficult to get
13 the price, but we knew that certain boards, we had to
14 give something to the boards, but there was no clear
15 process and programme in place to produce the price.

16 MR LANDERS: It wasn't said that, "We have had the
17 application, we must respond by X"?

18 A. No.

19 THE CHAIRMAN: We will come back at 2.10 pm, thank you.

20 (1.09 pm)

21 (The short adjournment)

22 (2.10 pm)

23 THE CHAIRMAN: Just a quick word on timing, Mr Cook. How
24 are we getting on, do you think?

25 MR COOK: I would anticipate another hour.

1 THE CHAIRMAN: Okay.

2 MR COOK: Mr Edwards, I see you have put everything away.

3 Could I ask you to get bundle 4 back out again, please,
4 and bundle 6. Bundle 4, tab 155. I'm afraid I have
5 a couple of questions that occurred to me during the
6 break.

7 You explain the origin of the management oncost.
8 Can I ask you to look back up at the top of D21 and the
9 explanation that was provided there. It says:

10 "In 1995/1996 breakdown of local costs for the
11 Ashgrove System was prepared in the context of the bulk
12 supply agreement ... This resulted in local costs being
13 estimated ... "

14 What you are describing now in terms of management
15 oncosts cannot publicly be described as local costs,
16 can it?

17 A. I think it was the costs of the company attributable to
18 that area. It wasn't a completely ring-fenced,
19 stand-alone cost of that system; it was the cost of us
20 running that system.

21 Q. If you look at the question:

22 "Please provide a breakdown of the actual costs
23 incurred by Dwr Cymru in providing the services
24 requested by Albion Water."

25 Quite simply, what you were providing there was in

1 no way at all associated with the actual costs
2 associated with Albion, was it?

3 A. As I said earlier, a lot of the actual costs of
4 providing support to provide this service were covered
5 in the overheads, and therefore the actual costs of the
6 system were far lower than it was -- that were actually
7 taking place to run the system. I believe these were
8 the actual costs -- what Mr Jones said in his witness
9 statement, he recognised this is a hybrid methodology
10 that's looking to say: if we looked at the
11 Ashgrove System on its own, how much do we think it is
12 costing us to run this system? And that would include
13 its fair share, or its share of costs of running
14 Welsh Water. That's what we were trying to do.

15 Q. You said "fair" share and then removed that word. Was
16 that because you recognised what you were trying to do
17 was a wholly unfair share of the costs?

18 A. I think it was a fair share based on the analysis.
19 There was no intent there.

20 Q. Can we go to tab 121 in the bundle, please? At page 853
21 we have here the breakdown of the costs that you
22 calculated for the purpose of the -- of course it's the
23 LCE paper, the second one that led to the first access
24 price. And we have the various headings, "Resource and
25 treatment distribution", items like that, and then we

1 have below what I would understand to be effectively the
2 add-on costs, the central office function costs,
3 customer services, scientific services, regulation and
4 doubtful debts. Those are the ones you were talking
5 about?

6 A. Part of them, yes.

7 Q. In terms of customer services, how many customers does
8 Welsh Water have?

9 A. In between 1.1 and 1.2 million.

10 Q. But you are suggesting that the costs of those customer
11 services, which reflect the fact that Welsh Water has
12 1.2 million customers, should be distributed by volume.
13 Is that what you are saying?

14 A. In D21?

15 Q. Yes.

16 A. I'm not sure what Dennis has done with customer numbers.
17 I don't know what is in the 6p.

18 Q. If you do not know what was in it, how could you have
19 said it was broadly right still?

20 A. It was a figure of the percentage order of what you
21 would expect the oncost to be.

22 Q. That's scientific services. Those are almost
23 exclusively to do with potable water, aren't they?

24 A. In the water service.

25 Q. Yes. So, again, there would be no reason for Albion to

1 be bearing any significant share of those, would there?

2 A. I don't know what was in the 6p.

3 Q. Doubtful debt, again, that's almost exclusively to do
4 with potable water, isn't it? Because there are
5 restrictions on the ability of water companies to cut
6 off water to retail potable customers, aren't there?

7 A. That's correct.

8 Q. So category of customer you are talking about here
9 almost exclusively arises from Welsh Water's potable
10 business, these million customers across the country?

11 A. I said these are part of the costs in there. Above the
12 line there is also a great deal of costs in the resource
13 and treatment and distribution that aren't allocated to
14 local cost centres. There is a big Ofwat (inaudible)
15 support on each of those lines, which are a fair
16 proportion of the costs that go into those attributed
17 costs. So the costs below the line.

18 The other element here is the operating profit, and
19 I think what D21 has done is put the company average
20 rate of return on the assets, which is spread over all
21 of the customers, whereas what we would expect to see
22 for a stand-alone system to large industrial customers,
23 a much higher cost of capital because of the risk of
24 those customers.

25 So I think there is an element in the hybrid D21

1 analysis which has benefited the stand-alone costs by
2 using the company average cost of capital.

3 Q. You accept that D21 has a separate provision for return
4 on capital, do you not?

5 A. Yes, at the company average level.

6 Q. If we go back to D21, tab 155, you had been asked to
7 provide, you were telling Ofwat you were providing local
8 costs. If you were going to allocate average costs
9 associated with categories that were about Welsh Water's
10 general business, that must have been something you
11 should have pointed out explicitly to Ofwat. That would
12 be the only fair way of presenting the information,
13 wouldn't it?

14 A. It was clear what we were doing there.

15 Q. No, it's not. The description you provided to Ofwat was
16 in 1996:

17 "In 1995/1996 a breakdown of local costs for the
18 Ashgrove System was prepared."

19 You are then suggesting that what you were actually
20 doing was including a great category of a volume-based
21 share of the average costs of the whole business, and
22 that is an extremely misleading description to provide,
23 isn't it?

24 A. I don't believe so.

25 Q. In terms of operating costs, if you look down, you'll

1 see in the Ashgrove entry, "Operating costs, Ashgrove"
2 and it's slightly over 2p; do you see that figure?

3 A. Yes.

4 Q. And then there were separate operating costs for mains
5 and telemetry. Did you bother to check the operating
6 costs figure?

7 A. I can't remember producing this table.

8 Q. If you go to bundle 6 again, Mr Jones' witness
9 statement, tab 241, in the back at page 1943.

10 Mr Edwards, if we simply refer back, we see D21, there
11 is a separate operating cost for mains and separate
12 operating costs for telemetry. So those are dealt with
13 separately.

14 If you look at page 1943, you will see that the
15 printout that Mr Jones produced, 2000 costs, show that
16 the operating costs for Ashgrove calculated at £354,000,
17 that include bulk water, £279,000, and we see the
18 calculation that's done across the page, which shows
19 that those operating costs are less than a penny per
20 metre cubed.

21 On that basis, again, you are putting forward
22 figures that were simply unrealistically high, weren't
23 you, in D21?

24 A. These were the figures from 1995/1994.

25 Q. You didn't carry out any checks at all, you would have

1 known that those figures were certainly not accurate in
2 the context of 2001?

3 A. If we did any checks at all.

4 Q. Did you do any checks at all?

5 A. I cannot recall.

6 Q. Thank you, Mr Edwards. I think you can put bundle 4 and
7 bundle 6 away.

8 Mr Edwards, I want to ask you some questions now
9 about indexation. As I understand your evidence, you
10 are saying that Welsh Water would have preferred --
11 sorry (Pause).

12 I was going to ask you some questions about
13 indexation. As I understand your evidence, you are
14 saying that Welsh Water's preferred price index for
15 water supply agreements was RPI?

16 A. That's correct, yes.

17 Q. And therefore you are saying that's what Welsh Water
18 would have wanted to include in any common carriage
19 agreement?

20 A. That's correct, yes.

21 Q. Yes. Do you recognise, of course, as with common
22 carriage that had to be justified by reference to costs,
23 indexation would also have to be justified by reference
24 to changes in costs, wouldn't it?

25 A. I assume so, yes.

- 1 Q. Yes. How had the costs actually changed?
- 2 A. The costs of the water industry changed on average by
3 RPI. That's why RPI is used in the price setting
4 methodology. It's recognised as the most effective
5 indexation to increase our costs by.
- 6 Q. Let's go and look to see, actually. We can remind you
7 of that. Go back to bundle 2, please. Forgive me
8 a moment. (Pause)
- 9 Sorry, Mr Edwards, I was going to take you to the --
10 if you recall, it was the document showing the changes
11 in price that we have been to before. The reference in
12 a moment.
- 13 A. The final determination?
- 14 Q. Yes, it was the final determination in 2000. You may
15 not need reminding by me taking you back to the
16 document. If you recall, though, that showed that it
17 was the costs of potable and sewage treatment that were
18 expected to go up, whereas the costs of the rest of
19 water was expected to fall by 25 per cent in real terms.
20 Do you remember I took you through that information
21 previously?
- 22 A. In real terms, yes.
- 23 Q. Yes. So while it might be right to say in terms of
24 potable costs that because they were improving standards
25 there was a need for those costs to go up, and RPI may

1 be a relevant measure to those, in the context of costs
2 excluding potable costs, which is what we are talking
3 about here, the expectation was that costs would
4 substantially fall in real terms.

5 A. In real terms or nominal terms?

6 Q. Real terms.

7 A. In real terms the implication of the final
8 determination, the P0, was to reduce the costs.

9 Q. It's not just P0, that's costs generally. In terms of
10 the non-potable element of costs, the expectation was
11 that those would fall substantially in real terms
12 because that was the 25 per cent figure I showed you?

13 A. In terms of the non-quality element of the system, yes.

14 Q. The non-quality element of the system, and non-potable
15 was a non-quality element of the system?

16 A. Yes.

17 Q. So the expectation would be that would fall
18 substantially in real terms?

19 A. In real terms, yes.

20 Q. So there was no possible justification for a non-quality
21 supply like this having indexation in accordance with
22 the measure that had no application to it?

23 A. What the FD is, is the K figure, which is the change
24 from RPI that would be expected. So the RPI is implicit
25 with the RPI calculation is -- that's how the costs,

1 nominally, would change and then the K factor was then
2 the real change.

3 Q. But if we are looking at a 25 per cent fall measured
4 over a five-year period, we are then talking about
5 5 per cent a year on average falling in real terms?

6 A. In real terms, yes.

7 Q. So you are talking, then, the non-quality element,
8 5 per cent below RPI?

9 A. The non-quality -- over five years, yes.

10 Q. 5 per cent a year over five years, yes.

11 So RPI for that period wasn't actually at
12 5 per cent, was it?

13 A. I can't remember exactly that period.

14 Q. It was simply, therefore, in those circumstances, no
15 possible justification in terms of costs-derived
16 measures for an indexation that was based simply on RPI,
17 was there?

18 A. The costs of the water industry are made up of half of
19 costs are operating costs and the other half are capital
20 charges and return on capital, and the return on capital
21 is very clearly driven by RPI because that's the RCV,
22 the regulatory capital value, and that's indexed by RPI
23 each year.

24 The element of capital charges is current cost
25 depreciation, which also moves by RPI, and then of the

1 50 per cent operating costs a lot of those cost are
2 people costs which tend to move by RPI and brought-in
3 services. So a great deal of those costs are driven by
4 RPI, which is the reason why RPI is used as the overall
5 measure of indexation for the water industry.

6 Q. Ofwat analysed your business and wholesale water, didn't
7 challenge that determination, did it, and the end result
8 of that analysis was to show that it expected your costs
9 to fall substantially over that period. I can take to
10 you the reference, it's bundle 2, tab 17, page 351B?

11 A. Sorry, what tab? Bundle 2?

12 Q. Tab 17, page 351B.

13 A. Sorry. Yes.

14 Q. We saw this before, if you look to the bottom of the
15 page and this is -- think about it being in real terms,
16 that:

17 Efficiency savings across the business were
18 expected to result in ...

19 There is a £76, about 25 per cent:

20 ... reduction in the average household bill and it
21 was only improvement in drinking water and environmental
22 quality, which are matters associated with either
23 potable water or sewage, which was expected to lead to
24 any increase in costs in real terms.

25 The points we have just been through.

- 1 A. I can see that, yes.
- 2 Q. So Ofwat had measured, therefore -- it expected that
3 efficiency had taken place in the past and was going to
4 take place in the future, which resulted in costs,
5 excluding potable water and sewage, falling by
6 25 per cent in real terms.
- 7 A. I accept that, yes.
- 8 Q. So against that background, there is simply no
9 justification at all for simply saying Albion should pay
10 RPI indexation, is there?
- 11 A. On that background there is less evidence, but on the
12 basis of the costs of the industry being -- the drivers
13 of the costs are RPI.
- 14 Q. The drivers might be RPI, but what Ofwat is saying is
15 actually you are managing to limit the items on which
16 you are going to have to pay any RPI and that's why you
17 get efficiency savings?
- 18 A. I think Ofwat had challenged us to hit those targets.
19 Those aren't what the costs are, but those are the
20 challenges Ofwat have set us.
- 21 Q. It's not a challenge, it's Ofwat's assessment of what
22 you should be able to achieve, and would achieve, and
23 which Welsh Water accepted as being viable because you
24 didn't challenge the determination?
- 25 A. That's correct.

1 Q. Yes. And this was the known background at the time when
2 you would have been negotiating common carriage, isn't
3 it, couldn't it?

4 A. At the time of the common carriage agreement, yes.

5 Q. To be clear, the time the common carriage agreement was
6 being negotiated?

7 A. Sorry, no, this was probably the year before that.

8 Q. I mean, so I suggest to you against that background you
9 couldn't expect to get an RPI indexation from Albion,
10 could you?

11 A. We would expect to get an RPI indexation from Albion,
12 yes.

13 Q. How could you do so when there was simply no
14 justification in terms of costs?

15 A. I believe there is a justification in terms of costs
16 movement.

17 Q. At the time that you were negotiating common carriage
18 with Albion, the existing agreement with Albion had been
19 in place for only two years. Are you familiar with
20 that?

21 A. Is this the 1999 one? Yes.

22 THE CHAIRMAN: I probably should know this. What does
23 "CSC's view of the company's strategy" mean?

24 A. Customer services committee.

25 THE CHAIRMAN: Is that something in Ofwat?

1 A. It was originally in Ofwat. At that time it may have
2 been separate from Ofwat. Each region had a customer
3 services committee that was the voice of the customers.

4 THE CHAIRMAN: I see, a consumer representative body?

5 A. Yes.

6 MR COOK: Mr Edwards, I was asking that you were familiar
7 with the fact that the existing agreement had been in
8 place for only two years, and at that time Ofwat has
9 indicated that indexation should not be higher than PPI,
10 or the increase in the potable carriage cost, and it
11 should be the lower of those two measures.

12 A. Ofwat had told us that, that's correct.

13 Q. Yes. So that was the top line of any acceptable level
14 of indexation, wasn't it?

15 A. No, that was specifically put place so that
16 Shotton Paper, when it was having the choice of being
17 supplied by Dwr Cymru or being supplied by Albion, could
18 make a choice on a level playing field. We wanted to
19 have an agreement for the bulk supply on RPI because
20 that was our standard -- preferred route, but Ofwat told
21 us we couldn't do that, to enable the customer to have
22 a fair choice, that we had to put PPI in the clause for
23 the bulk supply.

24 Q. It's broadly the same considerations applied at that
25 time as they did two years earlier, didn't they, in

1 terms of giving the customer the same measure of choice?

2 A. No, I believe common carriage was a completely different
3 entity.

4 Q. In terms of Welsh Water's contracts generally, I would
5 like to hand you up a document to have a look at once
6 again. (Handed)

7 A. Thank you.

8 Q. What we are going to do, Mr Edwards, is simply just go
9 through this in terms of the records that are in the
10 bundle. To be clear exactly -- because your evidence,
11 as I understand it, is you originally said there were
12 only three agreements containing PPI, and now I think
13 you accept there were four agreements around at the
14 relevant time?

15 A. There were 22 agreements of which four contained PPI and
16 the rest were either based on or relevant to RPI, and
17 one of them we didn't know. It was an old agreement.

18 Q. I think you summarise in your second witness statement,
19 paragraph 16, saying:

20 "The vast majority of special pricing agreements
21 entered into by Welsh Water post privatisation either
22 use RPI indexation or peg charges or movements in
23 charges to standard tariffs, driven by an overall RPI
24 plus K --

25 A. That's correct.

1 Q. Can I ask to you open up two bundles, please: bundle 4,
2 tab 163 and bundle 5, tab 214.

3 A. I have got bundle 4.

4 Q. Bundle 4, tab 163. Bundle 5, tab 214. In tab 163 at
5 the back of that tab, page 1022A.

6 A. Yes.

7 Q. I'm afraid we have to go to both of these because we
8 have in one page, 1340A, Special Agreements Register and
9 in the other we actually have the volumes sold, simply
10 so you can confirm when we go through what we are
11 looking at in terms of the contracts that were in place
12 at around that period.

13 So if we go to 1340A in bundle 5 -- that's the page
14 reference -- you will see there the Special Agreements
15 Register, and if we see the bottom of the page, the
16 first of those is the non-potable agreement, which is
17 WSHNONPOT 1, which actually starts over the page. We
18 can see in relation to that that that was indeed an RPI
19 index calculation, which I have included in the table.

20 Mr Edwards, I can take you through these in turn.
21 No doubt there will be a challenge in my figures if they
22 are wrong. Are you comfortable simply look at the
23 beginning sheet and somebody will tell you if I have got
24 it wrong in terms of these figures?

25 A. Yes.

1 Q. They both derive from going through the --

2 MR BEARD: We will wait and see, but that's not quite the
3 way that cross-examination works as a parlour game, as
4 I understand it. The idea that we should pop up each
5 time there might be a question.

6 THE CHAIRMAN: What you have done, presumably, Mr Cook is
7 you have added in the volume figures from page 1022A
8 into a list of the Special Agreements Register, 1340B?

9 MR COOK: Yes, I have.

10 THE CHAIRMAN: You have done that personally?

11 MR COOK: Yes, I have.

12 THE CHAIRMAN: I think we can proceed on the basis it's
13 probably accurate.

14 MR BEARD: Absolutely.

15 MR COOK: I can go through every single figure in turn --

16 THE CHAIRMAN: No, let's not.

17 MR COOK: Mr Edwards, what I have done is gone through the
18 register that we have there, identified those agreements
19 that are pre-privatisation and separately dealt with
20 those. You see I have gone 1 to 5. Those are post
21 privatisation, and the year date. There are three then
22 which are pre-privatisation, which I have put to one
23 side because they are pre-privatisation. Gone through
24 with the subsequent ones which, again, we can see the
25 identity of the accurate, the volumes, and then if we go

1 over the page of the sheet I have handed to you, down to
2 WSHNONPOT 13 of the ones listed in the Special
3 Agreements Register, and then we have the non-potable
4 bulk supplies.

5 Of course, before that we have the Shotton Paper
6 agreement, which is concluded in 1997, which was PPI or
7 change in volumetric charge, whichever was the lower,
8 which wouldn't figure on that because of course this is
9 the Special Agreements Register for 2000. By that stage
10 the Shotton Paper agreement had ended.

11 Then we have the bulk supply agreement, which is
12 actually Albion Water itself, which, again, was PPI or
13 change in volumetric charge, which you are familiar
14 with. And then we have the bulk 1 to Severn Trent,
15 which is non-potable. Again, that's pre-privatisation.
16 And also the one you have referred to where you say
17 there was an additional non-potable agreement, which you
18 say was PPI in your supplemental evidence.

19 That was what I have done there. I simply want to
20 ask you some questions based on that summary of the two
21 documents.

22 So in terms of looking through that, in terms of
23 agreements that were indexed by RPI, post privatisation
24 they appear to be what I have called number 1, or
25 WSHNONPOT 1. WSHNONPOT 2 was RPI as well. WSHNONPOT 4

1 was RPI, and then WSHNONPOT 11, number 08 on my list,
2 was also RPI. So those appear to be the four agreements
3 that are simply RPI. Do you see those?

4 A. Yes.

5 Q. In addition, there are two others that are linked, and
6 that's WSHNONPOT 12 and WSHNONPOT 13, which are linked
7 to changes in the potable tariff and were, therefore,
8 linked to RPI plus or minus K.

9 Can you help us -- I have added below WSHNONPOT 13,
10 which we understand should be the Corus Shotton
11 agreement. Our understanding is that between 1996 and
12 2000 that was a PPI-based indexation measure.

13 A. That's correct, yes. At 26p, yes.

14 Q. Sorry, at 26p. It wasn't at 26p during that period, was
15 it? It was 14p?

16 A. 26p. The 13?

17 Q. WSHNONPOT 13 is the Corus Shotton, so the steelworks at
18 Corus. I understand that was a PPI indexation, but the
19 price was 14p in that agreement until 2000?

20 A. No, that's not Corus Shotton.

21 Q. So what is not Corus Shotton?

22 A. 13.

23 Q. You don't believe it is?

24 A. No, I don't.

25 Q. But you understand that Corus Shotton was a PPI measure

1 until 2000?

2 A. I'm not sure what the Corus Shotton Paper was. That was
3 the agreement that expired in 1996 as well, was it?

4 Q. It expired in 1996, there was then a four-year interim
5 arrangement described in place.

6 A. I'm not familiar with the Corus Shotton.

7 Q. So looking, then, at those four that are RPI, two that
8 RPI plus or minus K. I mean, looking through them, they
9 are relatively small contracts on the whole, aren't
10 they? We start off with the smallest one,
11 non-potable 1, which is very small volume, 2,500-metre
12 cubed a year, then 140,000, then 1.3 million, and 12 and
13 13 are 2 million and 2.3 million respectively. I missed
14 one: potable 11, which is 3 million, then 2 million and
15 2.2 million are the RPI K contracts.

16 So looking at those it seems like RPI goes with the
17 agreements which are of smaller volume. Is that fair to
18 say?

19 A. I think it's the same as the non-potable bulk mains.
20 The numbers are associated with the lower volumes. The
21 actual driver for PPI was the timing that the
22 negotiation was made. The first agreement we had with
23 PPI was the British Steel stand-alone agreement, which
24 I think was 94, and then there were two or three other
25 agreements around that time that Mr Taylor negotiated.

1 We went in trying to get RPI and gave PPI as
2 a concession. So the reason that these companies are on
3 PPI is a factor of the time that the negotiation was
4 made, rather than the size of the works. Or the size of
5 the supply, sorry.

6 Q. But certainly, looking at this, if you look at entry 5
7 and of course Shotton Paper itself and Albion
8 subsequently, the two biggest non-potable -- and, of
9 course, WSHNONPOT 9, which is number 6 on my list, so
10 the three biggest customers, all had PPI indexation.
11 That's right, isn't it?

12 A. That's correct.

13 Q. In terms of the two that we see there, WSHNONPOT 12
14 and 13, which are the RPI plus or minus K, you see those
15 were agreed in 1999 and 2000 respectively, and that was
16 a point when Welsh Water must have known in relation to
17 2000, or suspected in relation to 1999 that there was
18 actually going to be a very substantial negative K
19 element over that five-year period, the next five-year
20 period?

21 A. Can I just -- I have just realised you were talking
22 about WSHNONPOT 13.

23 Q. Yes.

24 A. I apologise, I was talking about entry 13. That's why
25 I was confused. So I do apologise if I confused the

1 Tribunal.

2 THE CHAIRMAN: So you do accept that WSHNONPOT 13 is Corus
3 Shotton?

4 A. Sorry, yes. I do apologise.

5 MR LANDERS: When you said just now "I'm not familiar with
6 Corus Shotton", what do you mean by that?

7 A. I'm not familiar with the arrangements or the agreement
8 with Corus Shotton, as in what the agreement is.

9 MR LANDERS: At that time?

10 A. I'm not sure -- I'm not familiar with it now, as in what
11 the agreement is.

12 MR LANDERS: When you were working out the provision for
13 Albion, you didn't know what the Corus Shotton
14 price was?

15 A. I don't recall. I don't remember doing that calculation
16 or analysis.

17 MR COOK: I was asking you about WSHNONPOT 1 and 13.

18 A. Yes.

19 Q. Which were agreed in 1999 and 2000 respectively?

20 A. Yes.

21 Q. Saying at that point Welsh Water must have understood
22 that the K factor coming up was likely to be
23 substantially negative measured over the five-year
24 period?

25 A. At that time, yes. I think the key driver in the

1 negative was the first year. So it was negative for one
2 year and then broadly neutral.

3 Q. Yes. That was a 10.5 per cent reduction over one year?

4 A. That's correct, yes.

5 Q. So Welsh Water entered into an RPI, effectively
6 something that was by reference to its standard tariffs
7 and therefore an RPI K, knowing that the K there was
8 going to be a substantial negative number certainly over
9 the next year and then roughly level over the rest of
10 the four years?

11 A. Yes.

12 Q. So you knew then that was going to end up being
13 substantially lower than RPI itself?

14 A. That's correct, yes.

15 Q. Thank you, Mr Edwards. That's my questions on
16 indexation.

17 Mr Edwards, next capacity augmentation. Could I ask
18 you to go to folder 4, please, tab 126. Just to
19 clarify, I think you accept in your evidence that
20 Welsh Water didn't give a serious consideration at the
21 time for actual uses it could make of any surplus water
22 it had if it no longer had to supply Albion with that
23 water?

24 A. I don't think so, no.

25 Q. No. I'll take you actually straight to tab 143. I was

1 going to take you to the earlier correspondence, but
2 let's go -- and this is exchanges taking place between
3 Welsh Water and United Utilities, North West Water,
4 concerning whether or not there would be a need for
5 additional capacity if Welsh Water maintained its
6 36 megawatt-a-day capacity entitlement, but Welsh Water
7 was also supplying Albion with water.

8 If you can read the third paragraph on this page,
9 and then the fourth paragraph on the next page, please.

10 (Pause)

11 A. Yes, I've read the two paragraphs.

12 Q. Yes. So that was the recognition at the time, wasn't
13 it, that there was at the time no demand in excess of
14 that from Shotton Paper and Corus, and consequently any
15 investment in additional capital would be, in
16 North West Water's words, effectively wasted?

17 A. That's what John Lees put in the letter, yes.

18 Q. That was indeed the correct position, wasn't it? There
19 was no demand in excess of that of Shotton Paper or
20 Corus that could be supplied by Ashgrove?

21 A. There was no known demand at that time because there was
22 no spare capacity. We wouldn't have looked at that as
23 a suitable resource of water.

24 Q. It's not true to say there was no spare capacity. You
25 had the right to 36 megalitres a day and you were using

- 1 no more than about 26 on average.
- 2 A. On average.
- 3 Q. Yes. So there was a certain amount of surplus capacity
4 there?
- 5 A. There was an average surplus capacity, yes. I'm not
6 sure what the peak demand was and whether we could have
7 supplied other customers at the time of peak demand.
- 8 Q. And the system wasn't connected to any other customers
9 or the rest of Welsh Water's network, was it?
- 10 A. I think there was one small customer on, Bees Nurseries,
11 but apart from that, no, there wasn't.
- 12 Q. Bees Nurseries had stopped trading many years before,
13 hadn't it?
- 14 A. In that case there was none.
- 15 Q. So there was simply nothing that Welsh Water could do
16 with its 36 megalitres other than supply either Corus or
17 Shotton Paper?
- 18 A. At that time, no.
- 19 Q. It's right to say at that time as well that the
20 neighbouring resource zones had a substantial surplus of
21 water, didn't they?
- 22 A. I don't know, I haven't looked into that.
- 23 Q. And you can't give us any evidence of any economically
24 or environmentally realistic demand that Welsh Water
25 could have met with that additional capacity

1 availability?

2 A. I don't believe we did that investigation at the time.

3 Q. There was some consideration -- if we go to bundle 16,
4 tab 46. I hope you will find in your bundle -- it's not
5 in mine --

6 A. Water resources management plan.

7 Q. I hope you will find the water resources management
8 plan. This is Welsh Water's management plan for 2008,
9 and among the things that one finds considered in this
10 document were the theoretical options. Could I ask you
11 to turn within that to page 6672. What's being
12 considered is an assessment of feasibility options, and
13 among the things that are to be considered are -- it's
14 table 5.2:

15 "A tiered list of engineering options for each water
16 resource zone."

17 And we see there described what's being categorised
18 is in terms of the environmental criteria linked to the
19 SEA objective. Do you see that in paragraph 2 above the
20 table?

21 A. Yes, I do.

22 Q. The SEA objectives, what were they?

23 A. Strategic environmental assessment, I assume. It's the
24 nature of the report, but I don't know.

25 Q. And if we look through this, there does appear to have

1 been consideration of the technical feasibility of --
2 and if we go over the page -- it's five down from the
3 top:

4 "Zonal transfer from Alwen Dee using the Ashgrove
5 source works."

6 Do you see that?

7 A. Is this 6673?

8 Q. 6673. It's five down, it's the fifth line --

9 A. Sorry, yes, yes.

10 Q. And that was given a category of 3, so a very low
11 category of environmental desirability, didn't it?

12 A. I'm not sure what the categories refer to, but I confirm
13 it has got a three and an orange.

14 Q. We see above green is obviously, in the classic traffic
15 light system, most desirable and that's 1, and then
16 yellow, orange and red. We see that from the
17 description above it.

18 A. Yes, okay, yes, I would accept that.

19 Q. It was considered to be one of the most environmentally
20 undesirable options possible?

21 A. That's what the report is saying, yes.

22 Q. In terms of actually physically using the water,
23 Welsh Water would have to build a new pipeline taking
24 the water somewhere else, wouldn't it?

25 A. Or a new treatment works. Sorry, in order to use the --

- 1 as part of the network?
- 2 Q. Yes.
- 3 A. It actually would have to connect on to our network,
4 yes.
- 5 Q. It would have to have a new pipeline of some kind?
- 6 A. Yes.
- 7 Q. Unless you could find another customer that wanted
8 non-potable water, there would have to be some kind of
9 new -- either a connection to an existing treatment
10 works or a new treatment works built, wouldn't it?
- 11 A. Or a connection to a well water main going to
12 a treatment works. But, yes, that's correct.
- 13 Q. Physically none of those were available at the time,
14 were they?
- 15 A. None of those were available on the network at the time.
- 16 Q. Thank you.
- 17 I was going to ask you some questions next about
18 back-up potable costs. In terms of the costs, cost
19 arise, as I understand it, in terms of the back-up
20 potable supply to the extent to which that's actually
21 reserved capacity. If there is a reserved capacity,
22 that's something that Welsh Water actually has to hold
23 the ability available to supply that water on
24 a day-to-day basis?
- 25 A. Yes, it's the ability to be able to supply a large

- 1 volume of water, so it is a capacity charge, yes.
- 2 Q. Actually it's having it reserved, hold that capacity
3 available and making sure it's available whenever it's
4 needed?
- 5 A. It's a capability of supplying it very quickly, yes.
- 6 THE CHAIRMAN: Does that mean that there is actually a huge
7 pot of water somewhere, or does it just mean that you
8 have to take into account, when you are working out how
9 much of your water to use, that you might suddenly need
10 to use that reserved amount?
- 11 A. I'm sorry, this is right outside my knowledge of
12 operations. It's just an ability of a treatment works
13 to be able to supply that much water very quickly.
14 I don't believe it's having a reservoir available to
15 supply straight away. It's just the capability of the
16 treatment works.
- 17 MR COOK: If we can go to Ofwat's final determination of
18 2011, which you will find in folder 9, tab 304.
19 You are aware, presumably, this was an issue that
20 Ofwat had to consider in the context of the section 40A
21 determination. Are you familiar with that, Mr Edwards?
- 22 A. I'm familiar Ofwat have to deal with it. I'm not sure
23 what the section 48 determination is.
- 24 Q. Section 40A.
- 25 A. 40A. Is that the bulk supply agreement?

1 Q. It was the determination of the bulk supply agreement that
2 took place in October 2011.

3 A. Sorry, yes, I am aware, then.

4 Q. Could I ask you to turn in this to paragraph 6143. You
5 should be in tab 304, and then page 2745. This is
6 Ofwat's consideration.

7 Here we see potable water for back-up purposes,
8 price terms, and what we see here is Ofwat doing, just
9 below paragraph 6.129, is setting out the views of the
10 parties, he goes through setting out the views of Albion
11 initially, then Welsh Water, and finally we have just
12 above paragraph 6.141, Ofwat's assessment. And we see
13 at paragraph 6.143, it's an assessment of the issue of
14 the absence of the reserve capacity.

15 Start at paragraph 6.143. It says:

16 "We note Albion's clear statements that it does not
17 want the capacity for the potable back-up supply to be
18 reserved."

19 We see reference to an email being sent in the
20 context of that discussion at that time. Then 6.144,
21 Ofwat is saying:

22 "We have also taken [into consideration] the
23 relevant supply side considerations. Welsh Water notes
24 that had it treated the capacity potentially available
25 to Albion as reserved capacity in its water resource

1 management plan and the capital expenditure proposals it
2 made to Ofwat for the purposes of PR09."

3 That's the price review in 2009, isn't it?

4 A. That's correct, yes.

5 Q. " ... the result would have been the identification of a
6 supply deficit for the relevant water resource zone.
7 The identification of such a deficit would have had
8 implications for Welsh Water's capital expenditure
9 proposals. However, Welsh Water did not treat the
10 capacity potentially available to Albion as reserved in
11 its PR09 submissions and, accordingly, no provision was
12 made."

13 So looking at that, it's clear, isn't it, that
14 Albion was saying it didn't need it reserved and
15 Welsh Water in practice was operating on the basis that
16 the capacity was not reserved?

17 A. On the two sentences you read out. I'm not sure of the
18 context of the whole of this document.

19 Q. I mean, in terms of your knowledge, do you think that's
20 wrong?

21 A. I am not aware of the context of this, so therefore
22 taken to one and a half paragraphs out of context, I'm
23 not able to --

24 Q. Can you help us as to whether Welsh Water has ever in
25 practice reserved the capacity?

- 1 A. I think Welsh Water -- I think, as far as I'm aware,
2 Welsh Water has supplied the requests of the customer
3 when they require reserve capacity, which I would imply
4 it has got the capacity available.
- 5 Q. It's one thing to have it available if, effectively, you
6 want water around that day. It's another thing to be
7 reserving it so it's a guaranteed capacity. So you have
8 a bit of a treatment works standing idle ready to be
9 used if the capacity's required. Those are two quite
10 different things, aren't they, Mr Edwards?
- 11 A. I don't believe we run it as a special bit of
12 a treatment works only to be used whenever Albion Water
13 ring us up. I believe it's knowing that we have got the
14 capability of achieving the supply if it's ever
15 requested. So we don't keep assets specially for that
16 odd occasion that its required, if that was your
17 question.
- 18 Q. We saw in terms of what was being said in the extract
19 I took you to from the Ofwat determination, that had
20 Welsh Water being guaranteeing it could supply, it would
21 have needed to have additional assets to do so.
- 22 A. I don't think -- I think we make endeavours to supply
23 it, I don't think we do guarantee a supply.
- 24 Q. And the costs that you have been talking about in your
25 witness statement are only associated with a guarantee

- 1 reserved supply, aren't they?
- 2 A. I think it's associated with a volume -- there is a set
3 volume that we will make -- I think it's reasonable
4 endeavours to supply. So I don't think the guarantee is
5 there either in what I'm talking about.
- 6 Q. Can I ask you to turn back to folder 2, tab 8.
7 Folder 2, tab 8 should be the Ofwat minded to decision
8 of 1996?
- 9 A. The "Dear Jerry" letter?
- 10 Q. I believe it will be a "Dear Jerry" letter, yes.
- 11 A. Yes, I have got that.
- 12 Q. This is Ofwat setting out the reason why it had decided
13 that the price for non-potable water of 26p was
14 appropriate, and a price of 59p per metre cubed for
15 potable water. It says:
- 16 "It may be helpful if I explain the basis of this
17 recommendation. The price for potable water is based on
18 the cost of supplying large users as indicated to us by
19 Welsh Water and adjusted for inflation. This price is
20 also above the long run marginal cost of providing
21 water, as estimated by Dwr Cymru. The price for
22 non-potable water is similar to prices charged by
23 Welsh Water for other bulk supplies."
- 24 There is no indication in that context, is there,
25 that there is any additional costs associated with

1 having some form of reserved or guaranteed supply,
2 a dedicated supply?

3 A. Not in that paragraph, no.

4 Q. Are you aware of any evidence showing that Ofwat
5 included costs associated with having a dedicated supply
6 in the pre-existing pricing arrangement?

7 A. Pre-existing before 1999?

8 Q. Well, the matters that led to the agreement between
9 Albion and Welsh Water?

10 A. I have not studied those documents.

11 Q. So you can't provide any evidence saying there was any
12 element included in the price to take account of
13 dedicated or reserved capacity?

14 A. I'm not able to provide that evidence, no, but I'm not
15 saying there isn't any evidence.

16 Q. Can I ask you to turn to bundle 3, tab 78, please. This
17 was Mr Henderson to Mr Holton and also to yourself, the
18 9 November 2000 email. So it's the first one we saw you
19 were involved in, and he was setting out the position in
20 relation to volumes, which we see under paragraph
21 numbered 3. And we see at the bottom next to the two
22 bullets above it:

23 "We need to make clear to ELL [Albion] that ... we are
24 unable to guarantee a potable supply in the event of
25 a non-potable supply failure."

1 So that was the position that Welsh Water was taking
2 in the negotiations, wasn't it?

3 A. Sorry, whereabouts is that? Sorry.

4 Q. Sorry, it's at the bottom of the page.

5 A. Yes, I have got it.

6 Q. It's just above the bullet:

7 "We need to make clear to Albion ..."

8 And it's the final bullet:

9 "We are unable ... failure."

10 A. That's what I say. I don't think we have ever
11 guaranteed a supply -- reasonable endeavours.

12 Q. In the context of negotiations there was no question of
13 you being able to provide any form of guaranteed supply?

14 A. There was no guarantee. That's clear here.

15 Q. If I could ask you to just mention this point, if you
16 recall, that the potable supply for Albion is 59p. We
17 saw that a moment ago in the minded to decision.

18 If we could go now to bundle 2, tab 19. You do
19 remember that figure of 59p. If we can go to bundle 2, tab 15, which
20 is the Large Industrial Tariff.

21 A. Yes.

22 Q. If you were committing to provide some form of
23 guaranteed supply, if we look at the industrial tariff
24 breakdown, which we see at page 283, then the volumetric
25 price of water would actually have been substantially

- 1 below the 59p that Albion was paying, wouldn't it?
- 2 A. The 59p was determined by Ofwat based on our Large
3 Industrial Tariff. At that time this is the later Large
4 Industrial Tariff.
- 5 Q. Absolutely. So based on that later figures, if Albion
6 was going to be receiving some form of guaranteed supply
7 of volumes of water of the kind it would require, based
8 on its contract, then its volumetric price for water
9 would have fallen dramatically from 59p, wouldn't it?
- 10 A. For all water or just for the back-up supply?
- 11 Q. If it was getting some form of guaranteed entitlement or
12 contracting for a guaranteed entitlement for water, the
13 volumetric price would have been the highest or the top
14 band rate, wouldn't it?
- 15 A. No, because the way the Large Industrial Tariff works is
16 the fixed charge is calculated to make sure that over
17 the year you start getting the benefit of the lower
18 tariff by actually taking more money over the year. So
19 the break-even point is based on the 100 megalitres per
20 annum -- sorry, the 1,000 megalitres per annum. So if
21 you took 1,000 megalitres per annum and this volumetric
22 price, as the weighted average price would be lower, but
23 if you only took 500 megalitres and you were paying 41p,
24 you would actually pay more money. Does that make
25 sense?

1 Q. Yes, but you referred to the figure that Ofwat came up
2 with in the Tribunal proceedings. The Tribunal
3 concluded:

4 "It should not be ...(Reading to the words)... 4.4p
5 per metre cubed."

6 You are familiar with that?

7 A. Yes.

8 Q. And that was a figure referable to be added on to the
9 common carriage price?

10 A. That's correct.

11 Q. So taking account of the volume of water that Albion
12 takes annually, which is 26,000 megalitres, effectively
13 that equates to £300,000 a year. Again, I'm not asking
14 you to repeat my maths.

15 So looking at that time, if Albion was going to pay
16 £300,000 for a committed supply, that would entitle it
17 to a very substantial reduction in the price of water,
18 would it?

19 A. If they paid on the Large Industrial Tariff?

20 Q. It would be the only way to charge them if they were
21 going to pay £300,000 for a guaranteed entitlement?

22 A. I think the calculation of 4.4p was a calculation by
23 Ofwat of how much the capital reservation charge would
24 be for supplying -- is it 10 megalitres a day?

25 Q. Yes.

1 A. So 10 megalitres a day they worked out how much the
2 capital costs of the mains and the treatment works were
3 to supply that. They calculated that price on the
4 10 megalitres per day back-up supply and then averaged
5 it over the 18 megalitres supply, bulk supply. So
6 that's how they came up with the 4.4p.

7 Q. Mr Edwards, in terms of timing, can I ask you to turn to
8 your second witness statement, which you will find in bundle 1,
9 tab 6. At paragraph 50 you say based on your industry
10 experience and knowledge/discussions, you go on to
11 provide evidence about how long paragraph 51 -- and you
12 say -- you set out what in your view are the elements
13 that would have needed to take place. In paragraph 52,
14 you say:

15 "Based on that, it wouldn't have been feasible in
16 periods shorter than six months from the point in access
17 price was agreed."

18 A. That's correct.

19 Q. If we go back to paragraph 51, we can see the factors
20 you took into account. Paragraph D, you are assuming
21 that one of key factors that would cause delay would
22 have been the requirement for new engineering works,
23 haven't you?

24 A. Either engineering works or a different supply agreement
25 with Albion.

1 Q. And that's the key factor you are already saying would
2 make this take longer, as long as six months, to do?

3 A. I don't think so. The fact that it's D meant there are
4 other considerations.

5 I think United Utilities' position was not clear at
6 the time. It was clear to us they were looking -- for
7 these negotiations as a way of increasing their price.
8 They believed that the price that they were charging us
9 wasn't -- sorry, they believed -- sorry, they wanted
10 more money from us and they believed that this was
11 a method of achieving that money. And I believe that
12 was the biggest sticking point around UU using the
13 Competition Act to get the price for us increased
14 substantially.

15 Q. In terms of the matters that you can speak to, because
16 you weren't involved in the negotiations between Albion
17 and UU, were you?

18 A. I was not, no.

19 Q. So in terms of the matters you can speak to, which
20 appears to be A, C and D, can I just ask you some
21 questions about those?

22 A. Yes.

23 Q. So, A, how long would it have taken for agreement
24 between Albion and Welsh Water, not only on price but on
25 the remaining aspects of the common carriage agreement?

1 Could I ask you to take up bundle 3, tab 80, please.
2 I don't think we have been to this document before, but
3 it's a note, I believe prepared by -- Welsh Water's note
4 of the meeting on 10 November. We have mentioned
5 a meeting on 10 November 2000 before.

6 Just (inaudible), it starts off by saying:

7 "Suggest Paul E [Paul Edwards] is introduced as
8 competition team co-ordinator."

9 Is that an accurate description of your job title?

10 A. I was in the regulation team. I think I was financial
11 analyst at the time.

12 Q. Why were you being introduced by a different job title
13 than your real one?

14 A. I have no idea. Who wrote this? Does it -- do we
15 know --

16 Q. We don't know. Written by somebody within Welsh Water,
17 but apart from that, we don't know?

18 A. Right.

19 Q. It's setting out -- you see at the bottom of the page
20 "Response to ELL's proposal". Reference to where the
21 legal team had got at that time. Saying -- timescales
22 we see over the page, matters to be resolved, saying
23 target price to the end of December 2000. So at that
24 point -- and that was at the stage where you didn't even
25 have a methodology to produce the price because we saw

1 yesterday that was only at the end of November.

2 So at that stage Welsh Water were suggesting it was
3 a reasonable target to have an agreement in price
4 effectively within seven weeks?

5 A. I think what this document is doing is pushing for that
6 date. So that is a target date, yes.

7 Q. Yes. That was being put forward as a good faith target
8 date by Welsh Water?

9 A. Given that we hadn't got the price at that time, I think
10 what this was looking for was to see whether or not the
11 agreement could be completed.

12 Q. At that stage you were looking at it and saying, "We
13 still haven't go to the price element, but even taking
14 account of that, I think it's realistic to have a target
15 of only seven weeks away"?

16 A. That's what this document is suggesting.

17 Q. Any reason to think that was an unrealistic target?

18 A. At the time -- and we didn't have prices -- then I don't
19 think it's realistic.

20 Q. But that was the target that Welsh Water was putting
21 forward to Albion, wasn't it?

22 A. That was the target this document was suggesting, yes.

23 Q. And going back to your witness statement -- so that was
24 the agreement between Albion and Welsh Water. Then it
25 was paragraph C, paragraph 51C, where you say:

1 "Amendment of the Heronbridge Agreement between
2 Welsh Water and United Utilities."

3 You agree that that amendment is based on the
4 assumption that there would be a reduction in the volume
5 involved.

6 A. I think the issue -- this meeting was taking place
7 in November, and we had yet to meet -- the tripartite
8 meeting was early the next year. So this wouldn't be
9 aware -- at that time we wouldn't be aware of the full
10 position with UU.

11 Q. I had moved on from --

12 A. I'm saying that this is there. So that what I'm talking
13 about here is the fact that once we had had the
14 tripartite meeting, it was very clear that the views of
15 Dwr Cymru and the views of United Utilities were very
16 significantly different in the terms of the consequences
17 of the common carriage application for the bulk supply
18 agreement.

19 Q. Assuming there was going to be no change -- you accept
20 that if Welsh Water reserved its right to retain the
21 existing agreement, there was no need for a change in
22 the Heronbridge Agreement. If you maintain --

23 A. Yes, as far as we were concerned, if UU were willing to
24 offer the extra capacity to Albion Water and keep our
25 contract as it was, then there would be no -- it would

1 be ...

2 Q. And D, that's premised on the assumption there is going
3 to be capacity augmentation, or a new supply agreement
4 where Albion buys out Welsh Water's capacity
5 entitlement?

6 A. That's correct, yes.

7 MR COOK: Thank you very much, Mr Edwards, I have no further
8 questions.

9 Questions by THE TRIBUNAL

10 MR LANDERS: Can I just follow up from that last point. I'm
11 not sure I fully followed why you would have those sort
12 of discussions with United Utilities. Surely if you
13 agreed a common carriage with Albion, Albion would then
14 look for water either from you or from United Utilities?

15 A. That's correct.

16 MR LANDERS: And it would be in your interest to supply it,
17 because you were buying it at 3p and that would be
18 cheaper than Dwr Cymru was offering. So why wouldn't
19 you just do that? Sorry, United Utilities was efforts.

20 A. If Albion Water wanted to buy the water off us, which
21 was what they were doing at the moment.

22 MR LANDERS: But the price over and above common carriage
23 would just be that --

24 A. Which is what they are paying now, which would be the
25 service we were providing to them, yes.

1 MR LANDERS: If you had offered a lawful price and then
2 agreed a common carriage, that common carriage was in
3 place so that Albion then was faced with buying water
4 from either you or United Utilities, just for that
5 water, presumably you would offer whatever you were
6 buying it for from United Utilities plus a bit?

7 A. We would look to offer the regional average cost of that
8 raw water, but if that was in place, if they did have
9 common carriage and somebody came us and asked for
10 water, then we would look into it.

11 MR LANDERS: Sorry, in a commercial negotiation between
12 Albion, you and United Utilities --

13 A. Yes.

14 MR LANDERS: -- you wouldn't just treat that as a normal
15 competitive commercial negotiation of our costs are
16 whatever we are paying United Utilities and we would
17 just negotiate it, we would just have a trade off?

18 A. I think we would negotiate, but with reference to the
19 Competition Act in terms of what (inaudible) we were
20 negotiating. But I think we wouldn't not enter into an
21 agreement, so we would negotiate but under the sort of
22 auspices of the Competition Act and the condition E.

23 THE CHAIRMAN: Just a couple of questions from me. One of
24 the issues that emerged after Ofwat began its
25 investigation was the difference between dealing with

1 the matter on a whole company average basis and then
2 adjusting it to take account of certain circumstances
3 for this entrant, and looking specifically at the
4 Ashgrove System and what the costs of that were, and you
5 have said on a couple of occasions in your evidence what
6 you were arriving at in your calculations was not
7 a common carriage price for Albion to pay to use the
8 Ashgrove System, but a common carriage price that
9 Dwr Cymru would then offer to anybody who wanted
10 access -- common carriage on any part of the Dwr Cymru
11 network.

12 A. That's correct, yes.

13 THE CHAIRMAN: How did it come about that you personally, or
14 Dwr Cymru as a company decided that you were not going
15 to arrive at a common carriage price -- a bespoke price
16 for Albion to use the Ashgrove System, but that you
17 would arrive at a Dwr Cymru-wide common carriage price
18 which anybody who wanted then to come along and get
19 common carriage would be asked to pay?

20 A. I'm not sure who would have actually make that decision.
21 I think the concerns we had around condition E and the
22 Competition Act --

23 THE CHAIRMAN: I'm not looking for why that decision was
24 taken. I'm just trying to think about the process at
25 the moment. The exercise that you did was the exercise

1 of finding the general price, but was that something you
2 just assumed was what the company wanted you to do? Was
3 that something you suggested to Dr Boarer that you
4 should do? Was that something that Jeff Williams told
5 you to do? What discussions were there before you
6 started this whole number crunch -- before you and
7 Mr Henderson started -- because Mr Henderson was doing
8 that as well.

9 A. That's right, yes.

10 THE CHAIRMAN: He was just trying to find -- you were
11 dealing with different ways of doing that.

12 But how did it come about that you thought that was
13 the task rather than finding a price for Albion to use
14 the Ashgrove System?

15 A. I think it would almost be an evolution of the work that
16 Mr Taylor did. Dr Boarer became incomes manager in the
17 late 90s and she did the large industrial tariff, the
18 second one, so she would have inherited his thoughts on
19 the average tariffs and it would have developed from
20 there. I was never aware of a company policy written
21 down. I was never aware of a meeting where the decision
22 was made.

23 THE CHAIRMAN: So you were never present at any discussions
24 along the lines of, "How are we going to approach this
25 new task that we have of finding a common carriage

1 price?"

2 A. I think there were discussions around what options were
3 available with the ECPR, long run marginal cost, was it
4 long run incremental cost approach. So we were aware of
5 the different approaches we could take, and therefore at
6 that time there were discussions around which ones
7 should we do, but I think there was never a decision
8 made not to do what we had always done.

9 So I think the questions that the introduction of
10 the Competition Act was posing on the company were being
11 discussed. I think there was never a decision that we
12 would go to another type of costing. Therefore, the old
13 methodology would continue through. So I don't think
14 there was a conscious decision to keep through with it;
15 it's just a part of the DNA.

16 THE CHAIRMAN: I may have already asked you this, but I just
17 want to be clear what your answer is. As far, then, as
18 your going over Mr Henderson's work and coming up with
19 your own ideas as to how to do it, using, for example,
20 the average price rather than the volumetric potable
21 tariff, were those ideas that came out of a discussion
22 in a meeting where different ideas were bandied about,
23 "We could do it this way", "We could do it that way",
24 or were they things that you decided would be the right
25 things to do?

1 A. I think the change -- the document we saw with my
2 handwriting on it, that was me analysing what Paul had
3 done, and I can remember the meeting after I came back
4 from that where we discussed what I'd done and what Paul
5 had done, and it was considered that my way was the more
6 appropriate way.

7 THE CHAIRMAN: Who was at that meeting?

8 A. I was meeting Jeff Williams, Dave Holton was definitely
9 there, I'm not sure if Paul and Jackie were there, but
10 I definitely recall Jeff Williams and Dave Holton there.
11 And I would be surprised if Paul Henderson wasn't
12 because it was his paper they were discussing and
13 I turned up with my scribbles on it.

14 MR LANDERS: Just going back to the Chairman's previous
15 question, in the discussions you said right at the
16 beginning about LRMC and long run marginal cost, and so
17 on, were those conducted within your team? The
18 chairman, we know, was writing letters about the subject
19 at the same time as -- was there some sort of
20 connection? Was there a direction, or a leadership, or
21 a discussion, or an indication, or ...

22 A. I don't recall Dennis Taylor doing that when I was in
23 his team. So I believe those discussions would have
24 been led from Dr Boarer. So at that time, as Jeff was
25 being set up as the incoming director, it was Jackie's

1 area which Dave was reporting to Dr Boarer, and this was
2 that area they were starting looking at the different
3 prices we could charge.

4 MR LANDERS: As far as you were aware, there was never
5 a formal decision anywhere that these various options,
6 "We're essentially going to carry on as we were"?

7 A. I don't believe there was a formal decision not to do
8 anything else. So there was no formal ...

9 Further cross-examination by MR COOK

10 MR COOK: Sir, could I ask one supplemental question on the
11 Tribunal's question.

12 You said you didn't believe there was a formal
13 decision. Welsh Water's network access document that
14 was produced in August 2000, that included reference to
15 using average cost, didn't it? So that was the point;
16 presumably there was a formal decision made at that
17 point, tying it to that approach?

18 A. Yes, that would be the publication or the -- that would
19 be the case, yes.

20 Q. So that would be a formal decision taken at that stage
21 by somebody to do that? Who would that be?

22 A. I'm not sure where the network access code was approved.
23 It was done during August, but I'm not sure what level
24 that access code was approved.

25 THE CHAIRMAN: Any re-examination?

1 MR BEARD: I do have some re-examination. I'm also slightly
2 conscious of the shorthand writers. I'm probably going
3 to be 15 minutes.

4 THE CHAIRMAN: Let's come back, then, at 3.40.

5 (3.24 pm)

6 (A short break)

7 (3.40 pm)

8 Re-examination by MR BEARD

9 MR BEARD: Mr Edwards, I'll try to be relatively brief.

10 Just picking up from a question from Mr Landers just
11 before the short break, could you go to bundle 3,
12 tab 32, please, and turn to page 419. This is an
13 appendix to a letter from Mike Brooker. Could you read
14 through that page? (Pause)

15 A. Yes.

16 Q. Does that represent your understanding of the situation
17 at the time?

18 A. In December 1999?

19 Q. Yes.

20 A. Yes.

21 Q. If you turn back, you were cross-examined in relation to
22 parts of this letter, in particular the first and second
23 paragraphs on page 417. You were taken to those assumed
24 principles.

25 Just in relation to the third paragraph, could you

1 read that, please? (Pause)

2 THE CHAIRMAN: "There is a risk ..."?

3 MR BEARD: No, it should be:

4 "Crucially, MD154 ..."

5 I apologise, 417. My fault. (Pause)

6 A. Yes.

7 Q. You referred yesterday, just for reference, for the
8 transcript, page 140, lines 10 to 17 in response to
9 another question from Mr Landers, who had asked.

10 "Question: Did you say that this risk was likely as
11 a result of the introduction of the competition?"

12 "Answer: It was a risk as a result of the
13 introduction of competition, and one of the risks that
14 was identified in earlier papers was the -- I think it's
15 a letter from Mike Brooker in response to one of the
16 MD letters the fact that if we de-average then there's a
17 potential for cherry-picking. That was the point I was
18 making."

19 Is that the relevant letter you were referring to?

20 A. That's it. The first bullet or the penultimate bullet
21 point, yes.

22 Q. Thank you. There have been lots of references to
23 de-averaged pricing. What do you understand by
24 a de-averaged price?

25 A. A de-averaged price would be a stand-alone price,

- 1 a price for a specific -- so, start again.
- 2 A de-averaged price would not necessarily contain a fair
- 3 share of costs across a wide area. It would contain the
- 4 costs of either the local area or the point.
- 5 Q. So the local area or the point?
- 6 A. Yes, the point of whatever it was you were charging for.
- 7 Q. I think we may come back to that in a moment.
- 8 Could you turn on to tab 59 in the same bundle?
- 9 Mr Cook put various questions to you and, indeed, made
- 10 various submissions about the interpretation of this
- 11 document. Could you turn over to page 610, heading 2,
- 12 and if you could just read down and in particular to:
- 13 "Principles (v) ..."
- 14 (Pause)
- 15 What did you take that paragraph to mean?
- 16 A. I think that's the recognition by Ofwat that
- 17 de-averaging of prices leads to incidence effects.
- 18 Q. I think it might be worth just explaining, just for
- 19 clarity, what incidence effects, please?
- 20 A. The incidence effect is where companies -- sorry, where
- 21 customers are paying because of their accidents of
- 22 history, they are taking water that is relatively cheap
- 23 compared to average. Then an incident effect of
- 24 de-averaged pricing is they would get a reduced price,
- 25 and similarly, if a customer is in a rural area,

1 potentially with a high cost source of water, they would
2 then have to pay for that themselves and they would get
3 a much higher than average price. And the incidence
4 effect is moving customers from average to those prices.

5 So if you had a small community in North Wales with
6 a large pipeline and pump in would have a very
7 significant cost of their water, whereas somebody in
8 Cardiff would have a lot lower cost, but with us they
9 are paying the same. If we de-averaged then one would
10 be paying significantly more.

11 So that's the incident effect. It's just the change
12 in bill as a result.

13 MR BEARD: Sorry, Madam Chairman?

14 THE CHAIRMAN: Did you regard Heronbridge and the
15 Ashgrove System as a rural or an urban area?

16 A. I'm not sure I ever thought of it like that. The
17 area -- the actual area of the supply where it's
18 supplied to is heavily industrialised and the mains go
19 through rural areas. I think by "rural areas" we sort
20 of mean farming communities and small villages.

21 MR COWEN: Can I just --

22 MR BEARD: Of course, sorry.

23 MR COWEN: One thing. Your incidence effects and the
24 averaging depend on access to a network, don't they?

25 A. Yes.

1 MR COWEN: The fact that it's access to something that is
2 discrete, then those wouldn't apply, would they?

3 A. I think if you were to de-average over a large
4 conjunctive use system, then those customers would
5 expect to be charged the same as everybody else on a
6 conjunctive use.

7 In our more rural areas, where we have discrete
8 valleys, then they would be charged just on the single
9 network that they have. So, yes, you are right, the
10 de-averaging would go down the level of the network, if
11 that was the way we chose to do it.

12 MR COWEN: Thank you.

13 MR BEARD: Could you turn on to page 616, heading 6,
14 "Relationship with general tariff policy". Could you
15 just read the first paragraph of that? (Pause)

16 Can you just explain what you understand by that
17 paragraph, very briefly?

18 A. I think the recognition was that using clear de-averaged
19 tariffs would mean that some companies may lose
20 customers through cherry-picking, rather than by
21 an entrant who was more efficient, just being able to --
22 and in response to that, then companies would change
23 their tariffs and what -- I think what the regulator is
24 saying there is it has got to be done in a managed way,
25 or reasoned way if companies chose to do that.

1 Q. You were taken -- just to turn back to 611 to section 3
2 "Main approaches to access pricing", or I should say
3 more accurately the first section 3 because in this
4 document there are two section 3s. But the first
5 section 3, "Main approaches to access pricing" and it
6 was put to you there is only one way of reading these
7 sections.

8 I'm not going to rehearse the evidence you gave on
9 that, but did the other parts of MD163 and the
10 principles articulated there affect the way that you
11 read MD163?

12 A. I'm not sure I understand the question.

13 Q. If you go to the three paragraphs -- accounting costs,
14 long run marginal cost, efficient component pricing
15 rules -- access prices can be based on, it has been put
16 to you that there is only one way of reading that and it
17 must be the accounting costs directly related to the
18 particular assets to which access is sought. You
19 disagreed with that. But when you disagreed with that,
20 was it by reference to other parts of MD163 and in
21 particular the paragraphs that I have referred to?

22 A. The clear indication from the letter was that if any
23 company wanted to change the way it was -- they would
24 have to be very clear, the way of doing it.

25 THE CHAIRMAN: Did somebody within Dwr Cymru say to you,

1 "This is how we have decided to interpret it. We are
2 interpreting this to mean that the reference to the
3 assets to which access is sought is the whole network,
4 rather than the non-potable or potable networks,"
5 depending on the applicant, and rather than the actual
6 discrete pipes, if it's possible to identify those
7 pipes. Were you party to any discussions about how
8 to interpret this?

9 A. I can't recall that. I think the question would have
10 been the other way: does this preclude us from average
11 pricing? And we concluded from the support that the
12 regulator was clearly giving.

13 THE CHAIRMAN: When you say "we concluded", who did you
14 discuss that with?

15 A. At this time I would be working with Dave Holton, who
16 would have a clear brief to understand -- to make sure
17 we were compliant with these, and I think he would have
18 discussed it with me and Paul Henderson.

19 THE CHAIRMAN: So you and Paul Henderson and Dave Holton got
20 together and said, "Does this mean that we have to
21 change what we have done in the past?" "No it doesn't,
22 that's how we then go on and make our calculation"?

23 A. I think so. That was the type of conversation.

24 MR SHARPE: I'm sure my friend won't want to lead the
25 witness any further, will he?

1 THE CHAIRMAN: I'm probably leading him a bit now.

2 MR SHARPE: You are entitled to, madam, he is not, and he
3 knows it.

4 THE CHAIRMAN: Can I ask one more question? I'm asking you,
5 Mr Edwards.

6 When we looked at this before, and when you were
7 answering questions about de-averaging, there are stages
8 of de-averaging, aren't there? You can deal with the
9 whole company, you can deal the Ashgrove pipeline or the
10 specific assets, or you can say, "Let's have two prices
11 for common carriage, one for someone who is doing
12 potable common carriage and one for someone who wants
13 non-potable common carriage".

14 The price you eventually arrived at, the first
15 access price, was that a price for non-potable common
16 carriage, or was it a general price for either potable
17 or non-potable common carriage?

18 A. I think at the time this was out -- I remember thinking
19 at the time it was all potable. We hadn't considered
20 non-potable, and I think the first time we considered
21 non-potable was when the application came in September,
22 and therefore the drive for the first access price was
23 obviously the non-potable common carriage, but the same
24 principles, because we just wouldn't apply the
25 30 per cent, would mean that the common carriage for --

1 if someone wanted to common carriage potable water and
2 develop their own source for potable water, those prices
3 would be used for potable as well.

4 THE CHAIRMAN: But without the 30 per cent?

5 A. That's right, yes.

6 THE CHAIRMAN: So it would be a slightly higher price for
7 potable?

8 A. That's right, yes.

9 THE CHAIRMAN: But as far as the network was concerned, it
10 would still be the same whole network. You would create
11 or generate a difference in price because they are only
12 using the non-potable pipes, rather than only using
13 partial treatment?

14 A. No, the only distinction was the 30 per cent for the
15 partial treatment.

16 THE CHAIRMAN: Right.

17 MR COWEN: So when you said when this was being considered,
18 which was June 2000, there was no consideration of
19 non-potable on a discrete basis?

20 A. No, I think the recognition may have been there that we
21 needed to, but the statement of principles and the
22 network access code and the work we were doing with the
23 water industry through Water UK was totally geared
24 towards potable water, and I think a lot of the --

25 MR COWEN: Why was this document that we saw earlier today,

1 which had a consultancy study generated -- and
2 presumably that was generated some time in maybe July?
3 A. That was for the -- we recognised that the problems we
4 were having by not having a Large Industrial Tariff for
5 non-potable water. So what Paul was doing was trying to
6 develop a tariff. So that's why it was done.

7 THE CHAIRMAN: So that's why that study refers to a tariff
8 for non-potable water, rather than a common carriage
9 price, for example?

10 A. That's correct.

11 THE CHAIRMAN: Yes. So you were thinking that this was
12 going to all be people wanting accesses to the potable
13 network, and then in fact the first applicant comes
14 along and wants access to the non-potable network, and
15 then you had to decide how are we going to interpret
16 this reference to assets to which access is sought in
17 that context? Or that's not a question that you
18 remember people debating, or you debating?

19 A. I don't remember debating it once the -- once the
20 application had arrived.

21 MR BEARD: MD163 was an Ofwat document. What do you think
22 that Ofwat understood by MD163?

23 THE CHAIRMAN: He can say what Dwr Cymru understood.
24 I assume he would think that that was what -- I don't
25 know whether he can really look into the mind of Ofwat.

1 MR BEARD: It's not what Ofwat actually understood, because
2 obviously we have the Ofwat decision. I'm asking what
3 Mr Edwards thought Ofwat understood by MD163 because we
4 can go to the decision -- I'm going to go to the
5 decision for another reason in a moment because that
6 sets out what Ofwat thought about it.

7 A. I think one of the reasons why we would take note of
8 this document is, if ever we were to go before Ofwat on
9 one of these matters, we would want to be secure that we
10 were compliant. And I took this to mean that Ofwat were
11 not thinking about changing the way we were averaging
12 tariffs at the moment.

13 Q. It may be a convenient moment actually to take up
14 bundle 5/227. If you just turn on to 1493, just to get
15 the context from the heading. This is in the abuse
16 section and it's:

17 "Access pricing in the water industry."

18 And paragraph 240 sets out Albion's complaint, and
19 241 actually quotes a chunk of MD163, with which we are
20 familiar.

21 I won't take the Tribunal through 243/244, although
22 it's instructive. 245, under the heading "Average
23 accounting cost method used by Dwr Cymru":

24 "Dwr Cymru placed based the First Access Price on an AAC method,
25 or as Dwr Cymru called it, on a "whole company average basis"."

1 Is that an accurate characterisation of what you had
2 done in the FAP?

3 A. I think from my -- is this the --

4 Q. Sorry, this is the May 2004 decision that was
5 subsequently appealed before the Tribunal.

6 A. At the time I was doing it, I was not aware of the
7 average accounting cost terminology, but once the
8 decision had been published, then it was -- you know,
9 I recognised what I was doing with what Ofwat were
10 trying to do.

11 Q. Right. Then if we turn over the page -- this will be
12 a matter for submissions, but under the heading "First
13 access price", that's 1495, and if we turn on to 1498,
14 paragraph 257, could you just have a look at that
15 diagram? Does that accurately reflect your methodology
16 on the first access price?

17 A. This is the steps I referred to yesterday, when we went
18 through the methodology yesterday. I thought it was
19 a good representation, and in fact it's the one that
20 I use myself now to remind myself what I have done. So
21 I think it's a good way of presenting what I did.

22 Q. Right. Then there is consideration of your various
23 steps in the following paragraphs, but there is one
24 particular issue I wanted to raise with you because it
25 was the subject of cross-examination by Mr Cook, who

1 specifically talked about the exclusion of the
2 Elan Valley bulk supply agreement from step 1.

3 Is it your understanding that Ofwat considered this
4 issue when it was assessing the operation of step 1?

5 A. I think so. I think later on it explains why it
6 considers reasonable what I had done with the
7 Elan Valley bulk supply. I think is it 263? I think
8 they obviously did consider -- they understood what
9 I had done and they considered it.

10 THE CHAIRMAN: Although it seems to say that you not only
11 excluded the Elan Valley bulk supply agreement, but also
12 the second bulk supply agreement with Albion.

13 A. That's correct, yes.

14 THE CHAIRMAN: I don't think we got that from your
15 description of those schedules A to G when we were
16 discussing those, that went to the board.

17 A. The bulk supplies -- the lines I included was
18 measured/unmeasured, I think, and other, and the line
19 excluded was the third party, which were predominantly
20 bulk suppliers, which included small ones, Severn Trent
21 and Dee Valley, and I think this is one of the areas
22 that was identified by Ofwat that I shouldn't have
23 excluded that, and I should have included that in the
24 figures.

25 THE CHAIRMAN: So you decided, when you were coming to that

1 73p figure of the average price for water, rather than
2 the volumetric price that Mr Henderson had used, you
3 excluded not only the Elan Valley supply but also the
4 Albion supply?

5 A. Yes, I'm not sure I decided that, but that was the
6 consequence of what I have done.

7 THE CHAIRMAN: I don't understand that.

8 A. It wasn't a conscious decision to --

9 THE CHAIRMAN: You are not sure you decided --

10 A. I decided to exclude that line from the June return and
11 by excluding that line from the June return, it excluded
12 that --

13 THE CHAIRMAN: Did anyone within the company ever ask you
14 why you had excluded those two?

15 A. I can't remember. It's something that is quite
16 obviously wrong when you look at it like this.
17 Therefore, I can't imagine someone had ever looked at
18 that.

19 THE CHAIRMAN: Right.

20 A. One of the errors -- when I looked at it there were some
21 errors that I had made.

22 MR LANDERS: You had excluded all bulk supply, non-potables,
23 Corus at Llanwern and Corus Shotton and so on. Now, the
24 bulk supply is a supply from one undertaker to another.
25 So it was Severn Trent, Dee Valley. I think earlier on

1 we saw Wrexham was one, but that was Dee Valley later.

2 MR BEARD: In cross-examination it was suggested that in
3 relation to the unit cost of bulk water distribution,
4 the figure that you had used of 43.9p was flawed and
5 wrong. Did Ofwat disagree with the use of your figure?

6 THE CHAIRMAN: Just remind me what the 43.9 was?

7 MR BEARD: Actually it's easiest if you go back to that
8 diagram on page 1498. So it's the first figure on the
9 right.

10 MR COOK: I do apologise. This cross-examination proceeds
11 on an incorrect basis. I never challenged 43.9. 43.9
12 comes from the LIT price.

13 THE CHAIRMAN: No, it was the move from the 39p to the 39
14 something.

15 MR SHARPE: If my friend is persisting in leading questions
16 perhaps he could assist by giving the answers as well.

17 THE CHAIRMAN: It sometimes helps to clarify our thinking as
18 well, Mr Sharpe, so let's just see where we get to.

19 MR BEARD: I can assure Mr Sharpe there will be plenty of
20 submissions in due course in relation to these matters.
21 But I'm just trying to cover off matters that were dealt
22 with in cross-examination as swiftly as possible.

23 If you could turn on to page 1507, this is to do
24 with step 6, the settlement of the unit cost of
25 non-potable bulk water distribution. Could you just

1 read paragraph 300 at the top of 1508?

2 A. Yes.

3 Q. Do you agree with Ofwat's analysis in relation to those
4 matters?

5 A. I have no reason to disagree with them.

6 Q. Overall, from your understanding of this decision, did
7 Ofwat disagree with your interpretation of MD163 at all?

8 A. I don't believe they did.

9 Q. I think we can put away that document. Could we just go
10 to bundle 8, tab 274. This is what's referred to as the
11 Ofwat referred work. There was an exchange with Mr Cook
12 towards the end of the cross-examination that I confess
13 went fast for me. I don't know if it was the Tribunal,
14 to do with the back-up supply costs. If you turn on to
15 page 2334, you will see that there is a heading
16 concerning the inclusion of back-up supply and the three
17 methodologies.

18 So there was consideration of back-up supply in this
19 document. I think that's all agreed. Then one has at
20 2355 the authorities' approach to three issues common to
21 the methodologies. A third of those can be found at
22 2366, costing the back-up supply.

23 Could you just explain what you understand Ofwat
24 concluded in relation to the pricing of back-up supply,
25 just so we can be clear? This section concludes on

1 page 2376.

2 A. I think they undertook an exercise similar to ours where
3 they had taken proportion of the capital costs. I think
4 I have tried to explain this at the time, about potable
5 treatment and the proportion of the resource capital
6 costs. And they concluded that there was
7 a sufficient -- significant cost of providing the
8 back-up -- the capability of providing a back-up, and
9 that's what the conclusion is there, and therefore it
10 was worth -- it was material, so it needed to be
11 charged for.

12 Q. We know, of course, that the Tribunal said that that
13 cost should not be included in the common carriage cost,
14 but even if it's excluded from the common carriage cost,
15 is it a matter that you consider needs to be included in
16 any costs that will have to be paid by someone receiving
17 services from Dwr Cymru in relation to common carriage?

18 A. I think it's not a service we provide, typically.
19 Therefore, it would not be in the common carriage costs.
20 Therefore, if somebody want that service, I believe it
21 would be a separate service -- a separate cost.

22 Q. We have understood what AAC is, the whole company cost
23 approach. There is reference to AAC plus in that
24 document?

25 THE CHAIRMAN: My thinking processes are a bit slow, I'm

1 afraid. In all your calculations for the common
2 carriage price, you didn't include any element, or did
3 you include any element for back-up supply?

4 A. Not explicitly. I think the costs of that treatment
5 work would be in the average costs. The costs of the
6 average treatment work would be in the average costs.

7 THE CHAIRMAN: It's not the costs of the average treatment
8 work, it's the costs of having the reserve capacity. Is
9 that there somewhere in the figures that you would have
10 used?

11 A. The capital cost of the works -- the capital value of
12 works that was in -- the return on the capital value of
13 the works would be in the apportionment, and the return
14 that we were getting via the revenue would be included
15 in the cost. I haven't thought it through.

16 THE CHAIRMAN: All right. It's not very fair to ask you at
17 4.20 on a Friday afternoon.

18 MR BEARD: I'll leave that. I am, however, going to ask
19 a question about another term that has been used rather
20 a lot.

21 On a number of occasions you have referred to the
22 iDok and how important it was. Can you give any sense
23 to the Tribunal what a change in the iDok meant to
24 Dwr Cymru?

25 A. Do you mean what the iDok -- what the value of the iDok

1 submission was?

2 Q. Yes, because you have talked a lot about the importance
3 of that submission at the relevant time and I just want
4 to have a sense of what you were talking about.

5 A. The interim demonstration of K is a process of managing
6 extraordinary risks within a five-year period. There
7 were several very clear items we were allowed if they
8 materialised -- we were allowed to claim for. The claim
9 we put in was, I think, around £55 million over the
10 following four years.

11 THE CHAIRMAN: So what was the work that was going on at the
12 same time as you were doing this exercise?

13 A. That was the work -- it was a -- it's like a mini
14 periodic review we submitted in September. So we had to
15 prepare the submissions, and then between September and
16 Christmas Ofwat were asking us for various submissions
17 to support the evidence for supporting that claim.

18 THE CHAIRMAN: Is that September 2000?

19 A. Yes.

20 MR BEARD: Yes, the end of that year. I won't take you back
21 through the transcript, but reference to Mr Edwards
22 engaged in work in relation to iDok and the importance
23 of it. I just wanted to get the Tribunal a sense of
24 what that was really about, and I think 55 million over
25 four years is sufficient indication perhaps for these

1 purposes.

2 On a number of occasions you have also referred to
3 a concern that the methodologies or models or figures
4 that you were developing were robust for showing to
5 Ofwat. Why was it so important for Dwr Cymru to have
6 Ofwat's acceptance of what you were doing?

7 A. I think at the time Ofwat were feeling their way as
8 well. The reality was that the team set up in Ofwat,
9 the competition team, had not -- had not got experience
10 of competition, and therefore it was important for us to
11 share what we were doing with Ofwat and get feedback on
12 whether our interpretation of 163 were correct.

13 I think -- what I think at the time is Dwr Cymru, in
14 the period from January through to May, is Glas was in
15 fruition and one of the key elements there is the
16 support of the regulator for Glas. So the then owners,
17 WPD, were looking to sell the entity to Glas.
18 Therefore, we were very concerned at the time to make
19 sure that we had a good relationship with Ofwat.

20 Q. You also, in the course of talking about the Ofwat,
21 refer to the price control process on a number of
22 occasions. It was put to you at various points that
23 various of the different prices would give you, or
24 Dwr Cymru, a large profit. And just for the Tribunal,
25 that's not accepted by Dwr Cymru. But if that sort of

1 hypothetical profit had been available to you at those
2 prices, would you have been able to retain it over the
3 duration of a long contract?

4 A. The -- the income from a contract -- at each five-year
5 period, then the total income was measured on one side
6 of the periodic review equation and the costs were
7 measured on the other. And therefore, if we had a large
8 income from an industrial customer, then the requirement
9 for extra income from other customers would be less.
10 Therefore, in a sense we would not be able to retain
11 that level of income because it would be shared then
12 across the other customers.

13 THE CHAIRMAN: Did that mean in your experience that the
14 company didn't really mind whether it got income from
15 customers or not?

16 A. I'm not sure if "mind" is right.

17 THE CHAIRMAN: Did that affect their thinking in the sense
18 that they were not concerned with the amount of revenue
19 that they got.

20 A. No, I think we were very concerned with the amount of
21 revenue. At that time there was a team set up --
22 I think it was called the income maximisation team,
23 where we recognised that there were a lot of unbuilt
24 properties, so we put a lot of effort in increasing our
25 revenue.

1 So the increase in revenue was a good thing to go
2 for, recognising that after the -- at the end of the
3 periodic review process, at the end of five years, it
4 would be reset. I think Ofwat have now put in place
5 a revenue correction mechanism, which is trying to
6 address the sort of incentives inherent in that system.

7 MR COWEN: Just on that point, did you feel as part of the
8 organisation, that, you know, maximising income was the
9 sort of objective of the organisation? I'm also asking
10 a question about what your personal objectives were, if
11 any. What were you told to do? What did you understand
12 you were supposed to be doing.

13 A. I think my personal objectives were to make sure that we
14 had a good relationship with Ofwat. It was Ofwat
15 compliance. That was my objectives. I believe --
16 I would be surprised if Mr Williams or Dr Boarer hadn't
17 got some objective of income maximisation because that
18 was clearly their role.

19 THE CHAIRMAN: But as far as when you sat down in your
20 annual review, or whatever, with -- who was your boss?
21 Who did you have your appraisal --

22 A. I think that year I had it with Dr Brooker. Because
23 I had done the iDok with Dr Brooker, I had it with him.
24 But there was never any -- I did not receive a bonus, so
25 I was never incentivised in that way, and there was

1 never a goal towards --

2 THE CHAIRMAN: Did you ever have an objective that related
3 to this particular common carriage exercise?

4 A. I don't recall having one, no.

5 MR BEARD: I'm just going to move on to another definitional
6 point that I hope to clarify rather than confuse. There
7 have been lots of references to "stand-alone costs",
8 "average costs" and "local costs". Could we go to
9 folder 12, tab 13? Could you turn on to page 4051,
10 please, and could you read paragraph 424? (Pause)

11 It's just that paragraph. Do you recognise those
12 distinctions between stand-alone costs exercises and
13 local cost assessments?

14 A. I recognise the local cost and I understand what they
15 mean by stand-alone cost.

16 Q. Do you agree with what's said there?

17 THE CHAIRMAN: It's not something you can agree or disagree.

18 MR BEARD: It's really just trying to identify whether, when
19 Mr Edwards has been using the term "stand-alone costs",
20 he is referring to this sort of stand-alone costs
21 because there has actually been a degree of confusion in
22 questioning between stand-alone and local costs.

23 THE CHAIRMAN: I think that's a question which is useful to
24 ask him.

25 MR BEARD: Sorry, is this your understanding of the meaning

1 of "stand-alone costs"?

2 A. No, I think this is the first time I have seen this
3 definition. I probably use stand-alone costs and local
4 costs, as is said here, to mean the same thing.
5 I apologise if I have confused anybody.

6 Q. Could we just take up bundle 6/241. We are done with
7 folder 12. Could you go to tab 241, page 1918. This is
8 a statement of Chris Jones, the finance director. Could
9 we just go to 1918 and could you read paragraphs 5 to 8?
10 (Pause)

11 Is that what you understand by the concept of
12 stand-alone costs?

13 A. The way I read this is this is more of a hypothetical
14 situation, rather than the more hybrid element that was
15 in D21.

16 Q. Right. So you were cross-examined on page 1926, the
17 table there. Could you just turn back to paragraph 20
18 and read paragraph 20. (Pause)

19 Is that the way that a stand-alone costs exercise
20 could be carried out, in your view?

21 A. I think, given the definition you showed me earlier, of
22 the definition of the competition, the definition of it,
23 then this appears to be the way to do it, is to
24 establish what the hypothetical company delivering that
25 stand-alone system would cost.

1 Q. And then if you could turn on to the table at
2 paragraph 28, you were questioned about this in
3 comparison with the calculations that you had done that
4 concluded the management oncost. Would the fact that
5 this calculation was done on the basis of a hypothetical
6 stand-alone company affect the way these sorts of
7 calculations should be carried out?

8 A. In terms of this system, I would expect it to be quite
9 a simple company to run. Therefore, the management and
10 overhead would be quite low.

11 Q. Would it affect other aspects of the calculation as
12 well?

13 A. I think, as I said earlier, I think one of the big
14 concerns we would have with a small enterprise like this
15 would be the correct cost of capital.

16 Q. Could you turn back to paragraph 11 in this statement on
17 page 1920? Could you read paragraph 11, please? Do you
18 agree with that paragraph?

19 A. That's what I was trying to describe earlier. That was
20 the point I was trying to make earlier.

21 Q. Just to confirm, could you flip on to tab 244,
22 page 2052Q. This is an extract from the response to
23 questions posed by the Tribunal, but at 2052Q, you
24 referred in your evidence to a pie chart. Was that the
25 pie chart that you had in mind?

1 A. That was the one. I was hoping someone would shout out
2 where it was, but that's the evidence, yes.

3 Q. Thank you.

4 Earlier on today you were asked a question by
5 Mr Cook. I should say on my transcript it's page 82,
6 lines 14 to 17:

7 "Presumably you also know that as a result of that,
8 if the actual cost turned out to be significantly below
9 23.2p, then there is a very good chance that there would
10 be a finding of abuse against Welsh Water?"

11 To which you acceded. When you did so, what measure
12 of actual costs were you having in mind, when you gave
13 your answer?

14 A. I think it was a quantum rather than a measure I was
15 thinking of, if the number was a lot lower than the
16 23.2, if that was the context, and it was a quantum
17 I was concerned around rather than the methodology.

18 Q. Did you care whether any price that was offered would be
19 abusive?

20 A. I think that was one of the main aims of what we were
21 trying to do, was to make sure that it wouldn't be
22 viewed as abusive. So that was our main -- my main
23 thrust of doing all the work was to -- regulatory
24 compliance.

25 Q. Do you believe that anyone else at Dwr Cymru intended

- 1 Dwr Cymru to set an abusive price?
- 2 A. I can't think of anybody who would. I don't know of
3 anybody and I can't think of why anybody would want to.
- 4 Q. You were taken earlier to a document that was by Hyder
5 Consulting. Obviously, you have not had much chance to
6 review that. But on the basis of the information you
7 saw in that document -- I can take you to it if you
8 want -- would you be able to calculate a stand-alone
9 price for common carriage, just using that Hyder data?
- 10 A. I wouldn't be able to.
- 11 Q. What sort of other information or steps would be
12 required for you to calculate that?
- 13 A. I think all that was showing was the capital value of
14 the mains. So there is at operating costs, there is the
15 maintenance cost, or in terms of maintenance, we used
16 infrastructure renewals. So it would be an attributable
17 cost to that as well as a management oncost. There is
18 considerable -- other elements to include.
- 19 Q. Thank you. Could we just open up bundle 3, tab 110.
20 This is the Licence Company Executive paper which you
21 have been taken to in cross-examination. Could I just
22 take you down to number 2, "Recommendations". Could you
23 just read those bullet points, please? (Pause)
- 24 A. Yes.
- 25 Q. What did you understand to be the purpose of this

- 1 section of the Licence Company Executive paper?
- 2 A. I think what this was doing was informing LiCo what we
3 were doing and recommending that we carry on doing it.
- 4 Q. What in particular did you understand by the fourth
5 bullet, the calculate bullet?
- 6 A. I think that's the work I was doing. The constituent
7 parts would have been water resource, treatment, bulk
8 and local distribution.
- 9 Q. So did you understand that this was what you were to do
10 next, then?
- 11 A. What time was this? I think this is what we were
12 actually doing at the time. This is the 19.94, which
13 I would have calculated probably in December. So from
14 then I knew there was extra work to be done, so this was
15 saying that basically we carry on as we are, recognising
16 that we needed to improve what we were doing, make it
17 more robust.
- 18 Q. Thank you. Could you go on to --
- 19 THE CHAIRMAN: The final bullet there, the sixth bullet,
20 under "Recommendations":
- 21 "Establish the impact of prices developed for AW on
22 all other large users of non-potable water."
- 23 What did you understand that to involve?
- 24 A. I think this was basically the work that Mr Henderson
25 was doing to get the large non-potable industrial

1 tariff. So this was the work that I did, would
2 establish a price and methodology which would probably
3 inform that. So it was making sure that whatever Paul
4 was doing didn't diverge from what these numbers were
5 giving us. So I think this was recognising that the
6 two --

7 THE CHAIRMAN: This was the relationship between the common
8 carriage price and the proposed tariff for large users
9 of non-potable water?

10 A. Yes, I think, because Paul was doing it one way, I had
11 taken this on, but this then made sure that Paul would
12 have to make sure that whatever he was doing would have
13 to catch up with this now.

14 MR BEARD: Thank you. Could we put away bundle 3 and go to
15 bundle 4, please, tab 121.

16 MR COWEN: Just in terms of just your last answer, you said
17 whatever he was doing would have to catch up with this.
18 So you were focusing on this exercise in relation to
19 Albion and then going backwards over what he was doing,
20 not the other way round?

21 A. I think it was obviously undertaking this work in the
22 summer, which is what we saw in the Hyder Consulting
23 paper. So he was developing that methodology. Because
24 of this I had taken it and run off with it, then he
25 would have to catch up with where I was to make sure

1 that the two numbers were aligned, or the two
2 methodologies were aligned. That's what I meant by
3 that.

4 Sorry, which bundle, please?

5 MR BEARD: I'm sorry, bundle 4, tab 121. We are going to
6 couple of schedules you are very familiar with. Could
7 we just go to 852, schedule C? I'm just going to
8 explore a hypothesis that was put to you by Mr Cook.

9 Mr Cook put to you the proposition that you had
10 wrongly included some volume of raw water in the
11 non-potable water delivered row in schedule C. That's
12 the 119.85.

13 If you had done so -- and I'm not for a moment
14 suggesting it's wrong, but just going with Mr Cook's
15 hypothesis -- what would be the impact on the figures at
16 the bottom of that column, "The average cost of water,
17 1999/2000" and "The average cost of water 2000/2001"?
18 Would they increase or decrease?

19 A. The average cost of water, the volume is the
20 denominator. Therefore, if you increase the
21 denominator, the value would drop.

22 Q. If you decrease the denominator?

23 A. The average cost will go up.

24 Q. So if you removed some of the raw water volume, would
25 the average cost of water go up or down?

- 1 A. I failed miserably on this one the other day, didn't I?
2 If you remove the value, the average cost would go up.
- 3 THE CHAIRMAN: Doesn't that depend on what the price of that
4 water is?
- 5 MR COOK: Madam Chairman, again, I think this question
6 proceeds on the basis that I was suggesting that there
7 was wrongly included raw water in this. I don't recall
8 suggesting that. The questions I asked were if that did
9 include raw water. Of course it does; a lot of
10 non-potable water is raw. I wasn't saying that was
11 wrong in the context of this point.
- 12 MR BEARD: I may have misunderstood, but I remember the
13 words "financial trickery" being used in connection with
14 the inclusion of raw water. That seems to me to carry
15 with it a connotation of wrongfulness, even if the word
16 "wrong" isn't used. But maybe I'm being uncharitable to
17 Mr Cook. I will nonetheless pursue these questions.
- 18 Schedule B. If the average cost of water were to
19 have increased, what impact would that have on the
20 figure for water resource and treatment, 27.9p?
- 21 A. If the average cost increases, then the resource and
22 treatment at 38 per cent of the increased number would
23 be increased.
- 24 Q. And what would then be the impact on the water resource
25 and water treatment prices in the next section below?

- 1 Would they increase or decrease?
- 2 A. The water resource and water treatment below are a split
3 of that number, so they would both increase as well.
- 4 Q. And what would be the effect, then, on the non-potable
5 water treatment at 30 per cent of potable? Would that
6 increase or decrease?
- 7 A. The water treatment would increase. Therefore,
8 30 per cent of it would be an increased number.
- 9 Q. Thank you.
- 10 A couple more questions. You can put bundle 4 away.
11 Sorry, could you just bear with me for one moment?
12 I think I have the wrong reference. (Pause)
13 I'm sorry, it's bundle 18 -- not bundle 2 -- tab 5.
14 I apologise.
- 15 A. Bundle 18, tab ...? Sorry.
- 16 Q. Tab 5. In the course of cross-examination by Mr Cook,
17 it was put to you that the Corus price was 14p, on
18 a number of occasions the Corus Shotton price, and you
19 disagreed with that. Could you look at this letter,
20 17 February, from Mike Brooker. Do you have any reason
21 to disagree with what Dr Brooker says about pricing at
22 Corus in that letter?
- 23 A. No, I haven't.
- 24 Q. You can put in a bundle away and go to bundle 2, tab 15.
25 Just a point of clarification that I missed as I was

1 going through earlier. Page 283, paragraph 2.5. I'm
2 not sure much is going to turn on this, but there was
3 some cross-examination on this:

4 "Tariff will only apply to potable water users.
5 Tariff structure for non-potable users already reflects
6 a reduction in price per cubic metre due to lower
7 treatment and distribution costs. However, in the light
8 of the proposed new LIT, current standard non-potable
9 price is under review."

10 The "lower" there, what is it lower than?

11 A. Lower than potable users.

12 Q. Thank you.

13 One final question: if you had a large surplus of
14 water available to you at Heronbridge, would you,
15 Welsh Water, have sought to use it?

16 A. I think -- if we had a large volume of water at
17 Heronbridge, due to the nature of the contract it was
18 very, very low marginal cost, because of the fixed costs
19 element, the marginal costs was very low. Therefore,
20 when we are doing Water Resource Plan planning in the
21 area, I would consider that as one of our sources and it
22 wouldn't necessarily have to be an extra source, we
23 could use that rather than a more expensive source. So
24 if it was available because we knew it would not be
25 required for another customer, then we would look at it.

1 MR BEARD: Thank you. I have no further questions for you,
2 Mr Edwards. I don't know whether the Tribunal does?

3 Questions by THE TRIBUNAL

4 THE CHAIRMAN: How much did you know about the terms of the
5 Heronbridge Agreement at the time that you were doing
6 this whole exercise?

7 A. Me personally, I didn't know very much about them.
8 I know Mr Holton was engaged with the discussions with
9 UU, so he would have known them.

10 THE CHAIRMAN: One last question from me.

11 Dr Boarer, was she involved in this whole exercise
12 both because you were working on a common carriage price
13 and a non-potable large industrial users tariff, or was
14 she mainly concerned with the large industrial users
15 tariff aspect of what was going on there?

16 A. I think she was involved with both because Mr Holton's
17 reporting to her and she liked to be involved with all
18 the things that were going on on her team. She would be
19 involved for both reasons.

20 MR LANDERS: It just struck me that the answer you gave to
21 the previous question about Heronbridge, you are saying
22 that that water had a very low marginal cost?

23 A. Yes.

24 MR LANDERS: So it would be in your interest to use it?

25 A. If that was available.

1 MR LANDERS: Would that include selling it to Albion? You
2 were saying earlier that you would have to go through
3 the process laid down by section E, but in fact the
4 reality is if you got more than marginal cost, that's
5 what you would do, isn't it?

6 A. Subject to the --

7 MR LANDERS: Subject to regulation.

8 A. Yes.

9 MR LANDERS: I see.

10 A. We weren't free to just --

11 MR LANDERS: Give it away.

12 THE CHAIRMAN: Thank you very much, Mr Edwards. That has
13 been extremely helpful. I'm sorry it has been such long
14 days for you and very technical content, but it has been
15 very useful to have you there for a better understanding
16 of the figures in the documents. So thank you very
17 much.

18 A. Thank you.

19 THE CHAIRMAN: You are released from the witness box.

20 A. Thank you very much.

21 THE CHAIRMAN: I think that then brings this part of the
22 proceedings to a close. There are a couple of
23 outstanding bits of work that we are expecting from you,
24 one of which is a list of the actual prices paid by
25 Corus over the period so we don't have to try and guess

1 what it is. And then we will hear from you with your
2 closing written submissions, insofar as you want to put
3 something in writing, by close of play on the 1st, and
4 then we meet again at 10.30 on the 5th.

5 I think it would be useful if you could plot out how
6 those two days are going to be divided up between you
7 because we can't go over those two days, as far as the
8 panel is concerned, for closing submissions.

9 MR SHARPE: I think the understanding was, madam, that
10 I would close, my friend would then reply to my closing,
11 and in accordance with the Commercial Court practice,
12 which my friend commended to you, that I would have
13 an opportunity to reply.

14 So to ensure equality, I will probably finish
15 a little bit earlier on the Monday and my friend can get
16 up and say his bit and leave me a chunk of the afternoon
17 to reply.

18 MR BEARD: We will discuss timings, but that is the
19 essential structure, yes.

20 THE CHAIRMAN: Thank you very much to everybody. It has
21 been a long and complicated ten days, but thanks to
22 everyone for all their hard work in getting this case to
23 this stage.

24 (4.55 pm)

25 (The court adjourned until 10.30 am on 5 November 2012)

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