

Northumbrian Water responses to the Ofwat New Development Charging proposals (August 2016)

Q1 In light of our updates and clarifications, do you agree that we still retain the key features and approach of our March proposals?

We do agree with the general direction of the proposals, in particular the drive towards simplicity, transparency and cost reflectivity. We also favour the move from inflexible legislation towards more flexible guidance. Our only concerns over the proposals are in its implementation and a desire for a reasonable level of consistency in approach across the industry to help developers dealing with multiple water companies.

Q2 Do you agree with our updates and clarifications to our proposed rules?

The updates and clarifications are useful, for example, the clarification that developer charging is outside the IN16/02 wholesale charging rules process.

We also welcome the recognition that the degree of customer consultation should relate to changes in charges and be proportionate.

Q3 Do you agree that offsetting the infrastructure charge, rather than requisition charge, has merit? If so, when and how should this change be brought about?

Whilst we can see the merit in this proposal, we have concerns that such an approach may alter the total level of charges and the balance of charges for individual schemes.

This is most relevant for the sewerage service, where the income offset is generally unused given the low level of requisitions, yet infrastructure charges are collected in full. We agree with Ofwat's observation that this approach for wastewater would be best carried out from 2020, at which point a more rounded projection of costs and charges could be part of an overall Price Review.

For the water service, we are unclear whether such an approach is being mandated or merely suggested. Clause 29 of the charging rules suggests it is optional. Clarity on this would be helpful for all parties – different company interpretations of this with subsequent developer reaction could bring the new regime into question unnecessarily. We favour a mandated approach to avoid confusion.

Q4 Do you have comments on our proposed approach to implementing our rules?

In general, we are in favour of explicit, clear rules where Ofwat have taken decisions on a favoured approach. Whilst charging levels can be varied to reflect local conditions, we see no reason for there to be a multiplicity of charging approaches.

Q5 Do you agree with the approach we have taken to our draft impact assessment? Can you provide quantitative figures in terms of the potential benefits or costs? Is there anything we have missed?

We are comfortable that this exercise is worthwhile carrying out, if it is successful, the costs should be minimal and the savings due to greater certainty and less complexity should be considerable.

Q6 Do you have any comments on the drafting of our new connections rules?

Some drafting observations by clause:

11 If an undertaker is not applying fixed charges, then they are presumably variable according to a charge multiplier. We suggest saying ...Fixed Charges, the Variable Charge and the multiplier for that charge should be explained clearly,,,

17 We do not understand the reasoning for New Appointees to have a later deadline for Charging Arrangements. We are not aware that New Appointees require any charging information from other Appointees before setting their charges.

19 Whilst well-meaning, the reference to 'present balance of charges' is subjective – what will this phrase mean in 5 to 10 years time? We suggest a 'cost reflective' balance of charges would be a better term.

21 We suggest 'allow' rather than 'promote'.

22 This clause is very helpful, and should encourage a level playing field.

25 We welcome the first option for upfront fixed charges and we support the removal of the requirement to offer payments over time, with the associated administration costs.

26 The term 'physical infrastructure' is not helpful – we suggest 'the costs of providing the requisitioned Water Main' as this aligns to the WIAs43 definition. 'Physical' is an ambiguous word in this context.

28 The current wording states:

*28. Where an undertaker provides a Water Main or Public Sewer pursuant to a requisition and, in so doing, decides to increase the capacity of pipes or other infrastructure beyond that which is needed to meet the undertaker's duty..., the costs of this work shall be **apportioned** so that the person making the requisition only pays costs which are **in proportion** to the particular capacity required by his or her requisition.*

We have **serious concerns** over this wording as it contradicts the current Ofwat approach and could result in higher overall costs for developers and customers. The 'Wing Main' determination (25/8/15) states the following:

*Instead, we determined that these contributions should be equal to the **incremental** cost of the additional capacity of the Wing Main required for the new developments, to ensure that costs recovered reflect the costs reasonably associated with the provision of the relevant services.*

and

*3.45 The **incremental** cost is the difference between the actual and counterfactual costs that Anglian Water faced in building the Wing Main, and we assume that this is driven by the change in total capacity required between the two scenarios.*

We strongly agree with the approach taken under the Wing Main determination and it would be extremely unfortunate if that sensible approach were undermined by what we assume to be loose wording.

As the clause is currently worded, under a **proportion** approach, there is a strong disincentive for an undertaker to provide a main twice the capacity of the one required, even if that only increased the mains cost by 10%. We agree the developer should not pay '**more than they would otherwise have paid (the incremental approach)**', but we feel this approach inhibits the provision of capacity for future development, which is an important issue for UK Government and resilience purposes. It would also discourage provision of any headroom capacity, which could create significant re-laying costs or pressure issues should the customer's demand increase.

To align this clause with the Wing Main determination, we suggest rewording this as:

*28. Where an undertaker provides a Water Main or Public Sewer pursuant to a requisition and, in so doing, decides to increase the capacity of pipes or other infrastructure beyond that which is needed to meet the undertaker's duty under section 41(1) or section 98(1) of the Water Industry Act 1991, the **incremental costs of this work shall be excluded** so that the person making the requisition should only pay the costs that would have applied for laying a main or sewer of the capacity required by their requisition. ~~only pays costs which are in proportion to the particular capacity required by his or her requisition.~~*

29 We interpret this to mean a company could choose to apply an Income Offset to Requisition Charges, to Infrastructure Charges or not at all. If any of these choices are not allowed, conformation would be helpful.

We are surprised to see no reference to infrastructure charges in the charging guidance. A short number of clauses to confirm the right of undertakers to make such charges and that they should set these out in the charges scheme would seem appropriate. We note the reference to infrastructure charges in the charges scheme rules, but to separate these from the other charging rules seems unhelpful.

Q7 Do you have comments on the draft changes to the charges scheme rules?

The charging scheme rules appear to mostly apply to charges to households and non households for supply of services. The only section of relevance seems to be for Infrastructure Charges s26-32. We note that 32 (b) suggests that an undertaker MUST take account of previous usage. We agree, but note this seems to contradict the implied choice on pages 26-27 – this could be made more explicit we feel.

As per Q6, we wonder if Sections 26-32 might be moved or copied to the charging rules so all the new development guidance is in one place.

Q8 Do you have any comments on the drafting or our proposed licence modification, including the wording of the illustrative example.

We found Appendix 3 difficult to follow – Section 16.2 refers to connections under Section 18 of the Water Act 2014. We are not clear what this means. We hope it refers to the transitional schemes referred to in pages 41-42, where the previous arrangements continue to apply post April 2017.

**Northumbrian Water
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