

Meeting note

Friday 25th November 2016
Ofwat office, Bloomsbury Street, London
10.00am to 12.00 pm

New connection cost information sub-group – First Meeting

Attendees in person

Alex Whitmarsh	Ofwat
Mark Jones	Ofwat
Samuel Larsen	Thames Water
Heather Blamire-Brown	Affinity Water
Clare Lenoan	United Utilities
Paul Voden	Home Builders Association
Iain Amis	Anglian Water
Amy Johnson	Anglian Water

Attendees on the phone

Paul Fox	Ofwat
Martyn Speight	Fair Water Connections
Steve Wielebski	Home Builders Federation
Crawford Winton	Northumbrian Water

Apologies

Beverley Lawton	Bristol Water
Lynne Gibson	United Utilities
Ray Farrow	Home Builders Federation
Dave Mitchell	Home Builders Federation

Note of the meeting

Introduction

Alex Whitmarsh of Ofwat, welcomed everyone to the meeting and gave a brief overview of the purpose of the meeting, i.e. to discuss the draft Terms of Reference for the group and debate some initial thinking on potential data and approaches to monitoring as set out in the straw-man circulated to the group.

The group were then asked to share their expectations regarding the meeting which led into a general discussion around the topic, resulting in the following comments / discussions:

- Some concern was expressed by AFW/UU that the APR might not be the right place for capturing this information should forecast data be required. Ofwat restated the APR reports actual data for the reporting period only and should not reflect any forecast data. The comment was also raised that this group's mandate does not cover the charging rules themselves. If the group focussed purely on actuals then this will be less of an issue.
- A point was raised that there was a need to consider the range of accounting treatments and how disclosures are applied. Data needs to be meaningful and at the right level. Comparability is important.
- FWC emphasised the need for clear definitions - the slide pack was not clear when referring to the definition of infrastructure expenditure. It could be misinterpreted to include maintenance / infrastructure renewals which is not right and would not give rise to the one to one relationship we seek to monitor. Ofwat commented that the definitions cannot be clarified with certainty until the boundaries are finalised. HBF stated that stakeholders need to understand what the infrastructure charges have gone towards, with regards to reinforcing the network and in particular the split between water companies' contributions versus the contributions from other customers.
- Overall, there seemed agreement that it should be clear what funding comes from developers vs. other customers for expanding the network.
- HBF agreed to share their analysis on what proportion of network development costs seemed to be funded via the infrastructure charge (anonymising the water company on which the data is based).

Terms of reference

TMS welcomed the document. FWC stated that for the reconciliation to be meaningful and achieve a 'broad alignment' between costs/charges, the allowances for income offsets need to be known and defined. However, it was commented that currently the income offset is against the requisition charge and so would not form part of the new reconciliation of infrastructure revenue and costs and as such was outside of the scope of this meeting, although it was commented that it might be helpful to add a line for income offset at the bottom of the table on slide 10.

Maintaining the balance

ANH said that surely you need to know the current balance before you can maintain it. It's difficult to look back at what has happened historically, especially with regards to whether the balance is disproportionate or not. It was commented that historical analysis needs to be viewed with caution due to the change in accounting policies from UK GAAP to IFRS.

UU confirmed that they are doing some work on understanding their own historic balance and that this will inform their charging arrangements going forward.

HBA were concerned that we could be locking in an inappropriate balance of costs, if developers had been overcharged in the past. Ofwat's view was that our rules could allow the balance to change under certain circumstances, for example if there was evidence developers had been overcharged.

The group agreed that, although important, this activity is outside of the scope of the meeting.

Setting and resetting the infrastructure charge

The general view was that this should be considered as part of the WaterUK New Connections Working Group and not in this cost information working group.

ANH felt that although it is incumbent on all companies to provide data over a reasonable period, where there is more activity, there will inevitably be more movements in charges received and costs incurred. Thus some concern was raised regarding the additional burden involved in resetting infrastructure charges on an annual basis.

HBF commented that 70% of development sites have former use and wondered how this would be accounted for in the charges. Again, the general view was that this was a matter for the charging rules work rather than this group.

General objectives

All agreed that the information and monitoring needs to be adequate for customers and stakeholders and not too complicated or burdensome. It was acknowledged that there will be an additional burden on the water companies, due to the creation of new reports and potential system changes, but there is a need to strike the right balance. Furthermore, it was recognised that some companies have a limited number of resources involved in developer services.

FWC suggested that the 2017-18 transition year could provide an opportunity for companies to get used to this new reporting. This in turn would improve understanding for when the new charging rules come into effect in 2018-19. There was general agreement that it would be important to ensure the new approach needed to be right, but a range of concerns were raised about this coming in for 2017-18, especially the implications of incorporating it in the APR prior to the implementation of the new rules and whether this was really necessary. Suggestions regarding alternative approaches included the use of dummy data, a pilot by a small number of companies or to do nothing. prior to the implementation of the new rules

ACTION: Ofwat to consider what appropriate options are available in due course

It was agreed that the information must be appropriate, so as to allow for a meaningful reconciliation. From a developers point of view, the information must show where infrastructure charges have been expended. Commentary should be able to explain issues around timing and phasing and it was agreed that it should be proportionate to the relative size of the reporting organisation and value of the variance. ANH was keen to be able to show where investment has taken place ahead of need.

Straw man

Slide 6

The general agreement was that the preferred option was C – ‘Cost by process / activity’, as it was felt more appropriate from a data consistency and usefulness point of view.

Slide 10

FWC suggested that it would be beneficial if the slide (which supports option C, on slide 6), was amended to differentiate between site-specific costs and general network reinforcement. This would then allow a better reconciliation and understanding of costs. All agreed that clear definitions need to be constructed to aid understanding and its relationship with the charging diagram in slide 3, which will be addressed once the diagram has been finalised. It was agreed that the two current columns (providing new assets and Enhancing existing assets) be merged into a single column of Network reinforcement and a new column for site specific costs be added which would be for ‘memo only’ that would not form part of the formal reconciliation of infrastructure charges. Anglian suggested it might be helpful to add in contributions as an additional row at the bottom of the table.

Slide 11

TMS queried whether the reconciliation should be carried out on a cash or NPV basis. HBF confirmed that developers operate on a present day cost of accounting. The group therefore decided that it should adopt a similar approach and report on a cash basis for the sake of consistency and simplicity.

Slide 12

The general consensus was that option 2 was the most appropriate, showing costs and revenue and the split between water and wastewater. Must be mindful however, that there will be a wide variety of categorisations. ANH noted that there may be a difference that is both permanent and due to timing, but this could be covered as part of the supporting narrative.

Other comments

ANH floated the idea of whether a unit cost per connection would be useful for comparison purposes, say over a 5 year period? HBF were of the view that it would be unlikely that all the companies had the ‘right circumstances’ on which to draw meaningful conclusions from the unit costs. However, there was general support for

volume/activity information being included in the APR within the commentary to explain variances but not necessarily in a table. Such information would most definitely be included in companies' publications of their charging arrangements.

FWC felt that there should be a single table that is really focussed on the developer groups and would contain costs and projected activity such as the number of new connections and length of main laid. In effect, teasing out business planning information. ANH confirmed that length of main laid in their area is generalised based on average number of metres per plot, however acknowledging that there will be differences between companies.

HBF stated that Local Planning Authorities are required to publish predicted volumes of new connections. They update this with actuals on an annual basis, so the information is out there for water companies. ANH argued that 80% of LPAs publish these plans and in their experience, these are often aspirational. Rather than rely on them, ANH use them as an information reference.

UU and Affinity felt that the inclusion of forecasts was not necessarily appropriate for the APR and could cause difficulties when trying to obtain assurance over the data from their auditors. However, there was no objection to this information being captured in companies' narratives.

AOB

TMS asked how the process would account for network reinforcement work carried out by developers on behalf of the water companies and how this would get reflected / reported.

They wondered whether this meant that developers undertake work on behalf of water companies in the light green area on slide 3If the answer is yes they do, is this:

- One off activity or a regular occurrence?
- Company specific or industry wide?

In light of the above, they asked whether this should this form an agenda item for the next meeting.

On this issue, the HBA supported by the HBF, said that Ofwat have never qualified this element of competition. However, obtaining information from SLO's is outside of the scope of the cost information working group.

Overall it was agreed that it was a positive meeting and progress had been made.

Next steps / Actions

- Ofwat to circulate the notes of the meeting for comment / agreement
- Ofwat to updated an circulate the Terms of Reference and Cost Data Straw Man for further comment
- Ofwat to schedule a further meeting in the New Year to be held at their London Office. Proposal is Wednesday 18th January 2017 10.00am to 12.00pm